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No. 12633

2655

United States  
Court of Appeals  
for the Ninth Circuit.

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DAY-BRITE LIGHTING, INC., a Corporation,  
Appellant,  
vs.

RUBY LIGHTING CORPORATION,  
Appellee.

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Transcript of Record  
In Two Volumes  
Volume I  
(Pages 1 to 299)

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Appeal from the United States District Court,  
Southern District of California,  
Central Division.

FILED

NOV - 3 1950

PAUL P. O'BRIEN,  
CLERK





**United States**  
**Court of Appeals**  
for the Ninth Circuit.

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DAY-BRITE LIGHTING, INC., a Corporation,  
Appellant,  
vs.

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**Central Division.**





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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

### For Appellant:

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY,

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St. Louis 1, Missouri.

HARRIS, KIECH, FOSTER & HARRIS,  
WARD W. FOSTER,

JACK BARRY, JR.,

417 S. Hill St.,

Los Angeles 13, Calif.

### For Appellee:

C. A. MIKETTA,

WILLIAM W. GLENNY,

210 W. Seventh St.,

Los Angeles 14, Calif.

In the United States District Court of Southern  
District of California, Central Division

Civil Action No. 8381-M

DAY-BRITE LIGHTING, INC., a Corporation,  
Plaintiff,

vs.

RUBY LIGHTING CORPORATION, a Corpora-  
tion,  
Defendant.

COMPLAINT FOR INFRINGEMENT OF  
UNITED STATES LETTERS PATENT  
Nos. D-138,990 AND D-143,641

Plaintiff avers as follows:

First Count

I. Plaintiff

Plaintiff, Day-Brite Lighting, Inc., is a corporation duly organized and existing under and by virtue of the laws of the State of Missouri, and has a place of business in the City of St. Louis, State of Missouri.

II. Defendant

Defendant, Ruby Lighting Corporation, is a corporation duly organized and existing under and by virtue of the laws of the State of California, and has its principal place of business and a regular and established place of business in the City of Los Angeles, County of Los Angeles, State of California. [2\*]

### III. Jurisdiction

(a) The jurisdiction of this Court is based upon the Patent Laws of the United States of America.

(b) The acts of infringement hereinafter complained of were, and are being, committed in the County of Los Angeles, State of California, within this District, and elsewhere within the United States.

### IV. Title to Patent

On October 3, 1944, United States Letters Patent No. D-138,990 were duly and legally issued to Day-Brite Lighting, Inc., a corporation, Plaintiff, for an invention in Design for a Louvered Fluorescent Lighting Fixture, on the application of David J. Biller of St. Louis, Missouri, and Bertram A. Kaepfel of Normandy, Missouri; and said Plaintiff was at the time of the infringement herein complained of, and ever since the issue of said Letters Patent No. D-138,990 has been, and now is, the owner of the entire right, title, and interest in and to said Letters Patent No. D-138,990 and all causes of action for infringement thereof.

### V. Infringement

Defendant has been for a long time past, and still is, infringing said Letters Patent No. D-138,990 by making, using, and selling lighting fixtures embodying the patented invention and will continue to do so unless enjoined by this Court.

## VI. Notice

Upon information and belief, Plaintiff has placed the required statutory notice upon all lighting fixtures sold by Plaintiff under said Letters Patent No. D-138,990, and has given written notice to Defendant of its said infringement. [3]

## VII. Damage

Defendant has derived unlawful gains and profits from such infringement which Plaintiff would otherwise have received but for such infringement of said Letters Patent No. D-138,990, and Plaintiff has been greatly damaged thereby.

## Second Count

## VIII. Plaintiff

Plaintiff, Day-Brite Lighting, Inc., is a corporation duly organized and existing under and by virtue of the laws of the State of Missouri, and has a place of business in the City of St. Louis, State of Missouri.

## IX. Defendant

Defendant, Ruby Lighting Corporation, is a corporation duly organized and existing under and by virtue of the laws of the State of California, and has its principal place of business and a regular and established place of business in the City of Los Angeles, County of Los Angeles, State of California.

## X. Jurisdiction

(a) The jurisdiction of this Court is based upon



the Patent Laws of the United States of America.

(b) The acts of infringement hereinafter complained of were, and are being, committed in the County of Los Angeles, State of California, within this District, and elsewhere within the United States.

### XI. Title to Patent

On January 29, 1946, United States Letters Patent No. D-143,641 were duly and legally issued to Day-Brite Lighting, Inc., a corporation, Plaintiff, for an invention in Design for a Louvered [4] Fluorescent Lighting Fixture, on the application of David J. Biller of St. Louis, Missouri, and Bertram A. Kaepfel of Normandy, Missouri; and said Plaintiff was at the time of the infringement herein complained of, and ever since the issue of said Letters Patent No. D-143,641 has been, and now is, the owner of the entire right, title, and interest in and to said Letters Patent No. D-143,641 and all causes of action for infringement thereof.

### XII. Infringement

Defendant has been for a long time past, and still is, infringing said Letters Patent No. D-143,641 by making, using, and selling lighting fixtures embodying the patented invention and will continue to do so unless enjoined by this Court.

### XIII. Notice

Upon information and belief, Plaintiff has placed the required statutory notice upon all lighting fixtures sold by Plaintiff under said Letters Patent

No. D-143,641 and has given written notice to Defendant of its said infringement.

#### XIV. Damage

Defendant has derived unlawful gains and profits from such infringement which Plaintiff would otherwise have received but for such infringement of said Letters Patent No. D-143,641, and Plaintiff has been greatly damaged thereby.

Wherefore, Plaintiff prays for:

(a) A final injunction against further infringement by Defendant and those controlled by Defendant;

(b) An accounting and judgment for damages and for the profits of Defendant by reason of said infringement; [5]

(c) An assessment of and judgment for costs against Defendant; and

(d) Such other relief as the Court may deem just and proper.

Dated: At Los Angeles, California, this 29th day of June, 1948.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY,  
HARRIS, KIECH, FOSTER &  
HARRIS,  
WARD D. FOSTER,  
JACK BARRY, JR.,

By /s/ JACK BARRY, JR.,  
Attorneys for Plaintiff.

[Endorsed]: Filed June 29, 1948. [6]

[Title of District Court and Cause.]

ANSWER TO COMPLAINT

Defendant, Ruby Lighting Corporation, for its answer to the complaint, Admits, Denies and Alleges as Follows:

First Count

1. Defendant admits the allegations of paragraph I of the complaint.

2. Defendant admits the allegations of paragraph II of the complaint.

3. (a) Defendant admits the allegation of subdivision (a) of paragraph III of the complaint. [7]

(b) Defendant denies the allegations of subdivision (b) of paragraph III of the complaint and denies that it has infringed, either directly or contributorily, any claim or claims of any patent owned by the plaintiff, and denies that it has done any act or thing invading any right of any nature whatsoever of the plaintiff.

4. Defendant admits that United States Letters Patent No. D-138,990 were issued on October 3, 1944, but states that it is without knowledge or information sufficient to form a belief as to the truth of the other averments of paragraph IV of the complaint, and denies each and every of said averments.

5. Defendant denies each and every allegation of paragraph V of the complaint and specifically denies that it has infringed Letters Patent No. D-138,990.

6. Defendant admits that it received a notice dated August 12, 1947, accusing defendant of having

infringed patent No. D-138,990, patent No. D-143,641 and patent No. 2,411,952; defendant denies each and every of the other allegations of paragraph VI of the complaint.

7. Defendant denies each and every of the allegations contained in paragraph VII of the complaint.

And as Further and Affirmative Defenses, Defendant, Ruby Lighting Corporation, Alleges as Follows:

8. Defendant alleges that the alleged invention claimed in Letters Patent No. D-138,990 was not patentable to the alleged inventors named therein, under the provisions of [8] R.S. § 4929, § 4933, 35 U.S.C. 73, and that therefore said patent is invalid and void because:

(a) The alleged inventors, David J. Biller and Bertram A. Kaepfel, were not the original or first inventors of the alleged invention described and claimed in said Letters Patent or any material or substantial part thereof, but on the contrary that which is alleged to be patented by said Letters Patent and all substantial and material parts thereof were (if any invention were required) prior to the date of the alleged invention by the applicants for said Letters Patent, invented by others and more particularly those others identified in the following list, and the applicants for those patents identified in the following list;

(b) The thing or things alleged to be patented by said Letters Patent and all material and substantial parts thereof were patented and described



in printed publications in this or a foreign country before their alleged invention thereof, or more than one year prior to the date of application for said Letters Patent, and more particularly the patents and publications identified in the following list;

(c) The thing alleged to be patented by said Letters Patent and all material and substantial parts thereof were known and used by others in this country before said alleged inventors' alleged invention thereof, and more particularly by those others identified in the following lists, and the inventors named in the patents identified in the following list, and the assignees named in said patents, residing at the addresses stated in said patents; and [9]

(d) The thing alleged to be patented by said Letters Patent and all material and substantial parts thereof were in public use and on sale in this country for more than one year prior to the date of application for said Letters Patent, and more particularly by those identified in the following list, and by the applicants for and the patentees of the patents hereafter listed, residing at the addresses stated in said patents and publications:

#### United States Patents

Patent No.	Date	Name
D-130,809	Dec. 23, 1941	Waltman
D-131,845	Mar. 31, 1942	Biller
D-136,453	Oct. 5, 1943	Masterson
2,339,010	Jan. 11, 1944	Greenwald
2,364,992	Dec. 12, 1944	Maurette
2,411,952	Dec. 3, 1946	Biller

## Publications

1941 Catalog "Fluorescent Lighting," published by Ruby Lamp Mfg. Co., Inc., 430 West 14th Street, New York.

The defendant seeks leave to amend this answer to include other persons and corporations, patents and publications as soon as they are ascertained.

9. Defendant alleges that the Letters Patent in suit are invalid and void because the alleged invention purportedly described and claimed in said patent No. D-138,990 was merely the selection and adaptation of previously existing forms and devices within the powers of the ordinary designer; [10] that said alleged invention is not new, original, ornamental, and the product of invention as required by the United States patent statutes, rules and regulations pertaining to design patents; that the design lacks beauty, ornamentation and originality, and is only the necessary response to the purpose of the article, and the configuration thereof is necessary by function; and that the alleged invention is not the product of invention which is the purpose of the Constitution and patent laws to encourage and reward, and involves nothing more than the exercise of mere mechanical skill and the powers of the ordinary designer in view of the state of the art as known at the time and long prior to the alleged invention by the applicants for said Letters Patent.

10. Defendant alleges that the patent in suit No. D-138,990 is invalid and void because the Commissioner of Patents did not cause a proper examina-

tion to be made as to the alleged new invention defined by the claim of said patent, and had such an examination been made properly, it would have appeared that the applicants for said Letters Patent were not entitled thereto, and said Letters Patent would not have been issued, and that said Letters Patent were inadvertently issued.

11. Defendant alleges that the patent in suit No. D-138,990 is invalid and void because defendant is informed and believes and therefore alleges that the matters purporting to be covered by the claim of said patent were not the joint invention of the applicants for said patent but were the sole invention of David J. Biller, if any invention were required. [11]

#### Second Count

12. Defendant admits the allegations of paragraph VIII of the complaint.

13. Defendant admits the allegations of paragraph IX of the complaint.

14. (a) Defendant admits the allegations of subdivision (a) of paragraph X of the complaint.

(b) Defendant denies each and every of the allegations of subdivisions (b) of paragraph X of the complaint, and specifically denies that it has infringed, either directly or contributorily, any claim or claims of any patent owned by the plaintiff or in which the plaintiff has any right, title or interest.

15. Defendant admits that United States Letters Patent No. D-143,641 were issued January 29, 1946,

but states that it is without knowledge or information sufficient to form a belief as to the truth of the other averments of paragraph XI of the complaint, and denies each and every of said averments.

16. Defendant denies each and every allegation of paragraph XII of the complaint and specifically denies that it has infringed Letters Patent No. D-143,641.

17. Answering paragraph XIII of the complaint, defendant repeats and alleges as its answer thereto each and every of the allegations contained in paragraph 6 of its answer above set forth. [12]

18. Defendant denies each and every of the allegations contained in paragraph XIV of the complaint.

19. Defendant adopts, repeats and realleges as paragraph 19 of its answer to the Second Count of the complaint each and every of the allegations contained in paragraph 8 of defendant's answer above set forth, with like effect as if herein fully repeated but with reference to Letters Patent No. D-143,641.

20. Defendant adopts, repeats and realleges as paragraph 20 of its answer to the Second Count of the complaint each and every of the allegations contained in paragraph 9 of defendant's answer above set forth, with like effect as if herein fully repeated but with reference to Letters Patent No. D-143,641.

21. Defendant adopts, repeats and realleges as paragraph 21 of its answer to the Second Count of



the Complaint each and every of the allegations contained in paragraph 10 of defendant's answer above set forth, with like effect as if herein fully repeated but with reference to Letters Patent No. D-143,641.

22. Defendant adopts, repeats and realleges as paragraph 22 of its answer to the Second Count of the complaint each and every of the allegations contained in paragraph 11 of defendant's answer above set forth, with like effect as if herein fully repeated but with reference to Letters Patent No. D-143,641.

23. Defendant alleges that said Letters Patent No. D-143,641 are invalid and void because while the said application for said Letters Patent was pending in the United States Patent Office, the said application was amended, modified and changed, and the purported Letters Patent as issued relate to [13] another and different invention (if any) from that as originally filed.

Wherefore, Defendant prays:

1. That Letters Patent Nos. D-138,990 and D-143,641, and each of them, be held invalid, null and void.

2. That a judgment and decree be entered denying the plaintiff injunctive relief, and any relief whatsoever, and holding that this defendant has not infringed, and is not infringing, the Letters Patent in suit, and any of them.

3. That the complaint be dismissed, with costs and reasonable attorneys' fees to this defendant, and

that this defendant have such other and further relief as to this Court may seem just and proper.

Dated at Los Angeles, California, this 18th day of August, 1948.

KNIGHT, GITELSON &  
ASHTON,

By /s/ ROBERT R. ASHTON,  
C. A. MIKETTA,

/s/ C. A. MIKETTA,  
Attorneys for Defendant.

Receipt of Copy acknowledged.

[Endorsed]: Filed August 18, 1948. [14]

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[Title of District Court and Cause.]

### STIPULATION RE PROOF

It Is Hereby Stipulated, by and between the parties to the above-entitled action, through their respective counsel, and subject to the approval of the Court, that at the principal trial of this action Plaintiff need not prove the full extent of the recoveries to which it is entitled if the Plaintiff prevails upon the issues of patent validity and infringement, whether such recoveries be in the form of general damages, due compensation to the Plaintiff, reasonable royalties, costs, interests, attorneys' fees, or otherwise, but that such proof of the full extent of such recoveries may be presented after an interlocutory judgment of patent validity and infringe-

ment in such [15] proceedings as the Court may direct.

This stipulation is made to facilitate the progress of the trial of the principal cause.

Dated: At Los Angeles, California, this 10th day of June, 1949.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.  
HARRIS, KIECH, FOSTER &  
HARRIS,  
WARD D. FOSTER,  
JACK BARRY, JR.,

By /s/ WARD D. FOSTER,  
Attorneys for Plaintiff.

KNIGHT, GITELSON &  
ASHTON,  
C. A. MIKETTA,

By /s/ C. A. MIKETTA,  
Attorneys for Defendant.

Approved and It Is So Ordered, this 17 day of June, 1949.

/s/ JACOB WEINBERGER,  
Judge.

[Endorsed]: Filed June 20, 1949. [16]

[Title of District Court and Cause.]

## FIRST AMENDMENT TO COMPLAINT

The Complaint heretofore filed herein is hereby amended by adding thereto the following:

### Third Count

#### I. Parties

Plaintiff reasserts and adopts herein as fully as if set forth at length herein the allegations of Paragraphs I and II of the Complaint filed herein on or about June 29, 1948.

#### II. Jurisdiction

The matter in controversy exceeds, exclusive of interest and costs, the sum of Three Thousand Dollars (\$3,000.00). [17]

This action arises under the laws of the United States of America relating to unfair competition, including 28 U.S.C. 338 (b).

#### III. Creation of Business, Market and Demand

Plaintiff has for many years prior to the acts of Defendant herein complained of, built up and enjoyed a profitable business in the manufacture and sale of fluorescent lighting fixtures, and Plaintiff has spent large sums of money in advertising its said products throughout the United States.

As a result of its investment in preparing to produce commercially and in producing commercially and in large quantities its said fluorescent lighting fixtures, and as a result of the expenditure of much time and effort in promoting the sales of its said



products, Plaintiff has created and developed a large market and demand for its said products throughout the United States and a recognition of the merit of its said products and their dependability, and, as a result of such expenditure of money, time, and effort, the public recognizes Plaintiff's said products and their merit by their appearance.

#### IV. Defendant's Acts of Unfair Competition

Plaintiff alleges, upon information and belief that: Defendant is, and since prior to the filing of the Complaint herein has been, selling fluorescent lighting fixtures having the distinctive appearance of Plaintiff's fluorescent lighting fixtures, and Defendant has sold and palmed off upon the purchasing public and the members thereof, and the purchasing public and the members thereof have purchased from Defendant or wholesalers and jobbers purchasing from Defendant, such products of Defendant as and for Plaintiff's said products; and Defendant has in its said fluorescent lighting fixtures copied and [18] imitated the distinctive appearance of Plaintiff's said fluorescent lighting fixtures and has, by representations that its said products are the said products of Plaintiff and otherwise, appropriated the market and demand of the public for Plaintiff's said products created and developed by Plaintiff as the result of the expenditure of large sums of money, time, and effort as aforesaid; and Defendant has copied, imitated, and appropriated the distinctive appearance and appeal to the eye and esthetic sense of the purchasing public and the members thereof of Plain-

tiff's said fluorescent lighting fixtures and all of the non-functional elements and parts thereof; and such distinctive appearance and such elements and parts thereof have come to indicate to the purchasing public and the members thereof origin in Plaintiff of fluorescent lighting fixtures having such distinctive appearance and containing such elements and parts thereof by virtue of Plaintiff's expenditure of time and money in creating and developing said market and demand and in selling extensively throughout the United States its said fluorescent lighting fixtures.

Plaintiff alleges, upon information and belief, that: Defendant intends, and threatens to continue, to perform the acts complained of herein, unless restrained by this Court; the acts of Defendant complained of herein are related to and constitute a part of Defendant's acts infringing upon Plaintiff's patents as alleged in the first count and second count of said Complaint on file herein and constitute unfair competition with the Plaintiff and an aggravation of the damages to Plaintiff arising from Defendant's infringement of Plaintiff's said patents.

Wherefore, Plaintiff prays, in addition to the relief sought by the Complaint heretofore filed herein, for:

(i) A final injunction against the Defendant, restraining the Defendant from the performance of the acts of unfair [19] competition alleged in this First Amendment to Complaint;

(j) An accounting for the profits realized by Defendant from the acts of said Defendant com-

plained of in this First Amendment to Complaint;

(k) An assessment of costs and an allowance of judgment for attorneys' fees against Defendant; and

(l) A judgment for such other and further relief as to the Court may seem just.

Dated: At Los Angeles, California, this 1st day of March, 1950.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.

HARRIS, KIECH, FOSTER &  
HARRIS,  
WARD D. FOSTER,  
JACK BARRY, JR.,

By /s/ WARD D. FOSTER,

Attorneys for Plaintiff. [20]

Upon the application of Plaintiff by its counsel, and good cause appearing therefor,

It Is Hereby Ordered that the Complaint on file herein may be, and the same hereby is, amended by the First Amendment to Complaint, copy of which is attached hereto, and permission to file which is hereby granted.

Dated: At Los Angeles, California, this 1st day of March, 1950.

.....,  
Judge.

Lodged March 2, 1950.

[Endorsed]: Filed March 3, 1950. [21]

[Title of District Court and Cause.]

ANSWER TO FIRST AMENDMENT  
TO COMPLAINT

Defendant, Ruby Lighting Corporation, for its Answer to the First Amendment to Complaint, admits, denies and alleges as follows:

1. Defendant admits the allegations of Paragraph I of the First Amendment to Complaint.
2. Defendant admits the allegations of Paragraph II of the First Amendment to Complaint.
3. Defendant denies each and every allegation of Paragraph III of the First Amendment to Complaint.
4. Defendant denies each and every allegation of Paragraph IV of the First Amendment to Complaint. [22]

Wherefore, defendant prays, in addition to the relief sought by the Answer heretofore filed herein,

1. That a judgment and decree be entered denying the plaintiff's injunction relief, and any relief whatsoever, and holding that defendant has not committed acts of unfair competition against the plaintiff.
2. That the defendant be awarded his costs and reasonable attorney's fees and such other and further relief as to this Court may seem just and proper.



Dated at Los Angeles, California, this 6th day of  
March, 1950.

KNIGHT, GITELSON &  
ASHTON,  
C. A. MIKETTA,  
/s/ C. A. MIKETTA,  
W. W. GLENNY,  
/s/ W. W. GLENNY,  
Attorneys for Defendant.

Receipt of Copy acknowledged.

[Endorsed]: Filed March 6, 1950. [23]

At a stated term, to wit: The February Term, A.D. 1950, of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Wednesday, the 22nd day of March, in the year of our Lord one thousand nine hundred and fifty.

Present: The Honorable James M. Carter,  
District Judge.

[Title of Cause.]

### MINUTE ORDER

This cause having been tried by the court, and the court having heretofore ruled on all issues except unfair competition, and that issue having been taken under submission, and the court having duly considered the matter, the court now finds in favor of the defendant and against the plaintiff on the issue of unfair competition, and orders that judgment be accordingly.

Counsel for defendant will prepare and present proposed findings of fact, conclusions of law and judgment on all issues, pursuant to local Rule 7, within ten days.

[Title of District Court and Cause.]

AFFIDAVIT OF C. A. MIKETTA  
RE ATTORNEYS' FEES AND COSTS

State of California,  
County of Los Angeles—ss.

C. A. Miketta, being duly sworn, deposes and says that he is an attorney at law, counsel for defendant Ruby Lighting Corporation in the above-entitled action, and has personally handled and is familiar with all of the proceedings had in such litigation.

That plaintiff originally charged defendant Ruby with infringement of two design patents and a mechanical construction patent No. 2,411,952 (plaintiff's Exhibit 5); that affiant made an investigation and study regarding said patent No. 2,411,952, reported the results thereof to plaintiff and defendant and the [25] plaintiff dropped the charge as to patent No. 2,411,952. That plaintiff took depositions of five of defendant's officers and employees, which depositions were not introduced into evidence by plaintiff during the trial of the action.

That affiant and his associate have worked a total of 406 hours on the above case, including location and study of prior patents, publications and catalogues, analysis of plaintiff's patents and defendant's devise, legal research, preparation of answer, appearances in Court on call of calendar, considering and entering into stipulations, attendance at taking of depositions of defendant's officers and

employees by plaintiff, preparation of pretrial memoranda and points and authorities, preparation of answer to first amendment to complaint, preparation of memoranda on alleged unfair competition, and time and services during trial on February 28, March 1, 2, and 3, 1950.

That the reasonable and fair value of the services rendered and for which defendant has been billed is \$6,240; that defendant has paid about one-half of same sum prior to trial; that the disbursements for reporter's fees, photostats, file histories, blueprints and exhibits in connection with this case, which have been paid heretofore by defendant amount to \$684.13, whereby the defendant has incurred costs and expenses as a direct result of plaintiff's action of \$6,924.13 and prays recovery thereof.

Dated this 29th day of March, 1950.

/s/ C. A. MIKETTA.

Subscribed and sworn to before me this 29th day of March, 1950.

[Seal]     /s/ MILDRED K. BADGER,  
Notary Public in and for the County and State  
Above Named.

My Commission Expires Mar. 2, 1952.

Receipt of copy acknowledged.

[Endorsed]: Filed March 30, 1950. [26]



[Title of District Court and Cause.]

FINDINGS OF FACT AND  
CONCLUSIONS OF LAW

This cause coming before the Court for trial on final hearing and trial being had on February 28, March 1, 2 and 3, 1950, during which witnesses were heard, demonstrations had and observed by the Court, exhibits filed and considered, briefs and memoranda having been filed and oral argument had, the Court, having rendered its decision and being fully advised in the premises, does hereby make the following Findings of Fact and Conclusions of Law:

Findings of Fact

1. Plaintiff, Day-Brite Lighting Corporation, Inc., is a Missouri corporation engaged in the manufacture and sale of fluorescent lighting fixtures. Defendant, Ruby Lighting Corporation, is a California corporation having a regular and principal place of business at Los Angeles, California, and is also engaged in the manufacture and sale of fluorescent lighting fixtures.

2. Prior to the filing of the complaint herein plaintiff charged defendant with infringement of United States Letters Patent No. D-138,990, No. D-143,641 and No. 2,411,952, by written notice dated August 12, 1947. Plaintiff's complaint, as filed, charged defendant with infringement of United States Letters Patent No. D-138,990 and No. D-143,641 and the first amendment to the complaint,

filed at the end of plaintiff's prima facie case, charged defendant with unfair competition.

3. The patents in suit are patents for designs for fluorescent lighting fixtures, issued under the provisions of R.S. 4229, 4933 (35 U.S.C. 73). Patent No. D-143,641 (plaintiff's Exhibit 4) was filed July 28, 1944. The file history of this patent shows that the application for patent was originally rejected by the Patent Office upon the ground that the design was not inventively different from the design of "Challenger No. 77" fixture, and applicants distinguished from such prior art fixture by calling attention to their use of a V-shaped longitudinal louver having a hollow longitudinal bottom bead of circular cross-section, the use of specular metal for such V-shaped louvers, and notched upper edges in cross louvers which are reflected in the specular V-shaped louver.

4. More than one year prior to the filing of the application for United States Letters Patent No. D-143,641 there were published and known in the United States, fluorescent lighting fixtures having bottom light-emitting openings provided with longitudinal and transverse louvers, as shown by the "Challenger No. 77" fixture, and by other prior fixtures not considered by the Patent Office, including those illustrated in patents and specifications forming a part of defendant's Exhibit I and particularly subdivisions 1, 2, 4, 6, 7, 9, 10, 12, 17, 21, 22 and 23, thereof. [29] Some of these prior fixtures included V-shaped longitudinally extending louvers.

5. Patent No. D-138,990 (plaintiff's Exhibit 3) shows a fluorescent lighting fixture having the same longitudinal and transverse louvers as appear in patent No. D-143,641 and in addition, a step-down end portion having a zigzag ornamentation in its lower portion, and a protruding upper portion provided with a central boss; the upper and lower rails of the side panels are connected by three parallel bars integral with the upper and lower rails. The file history of this patent shows that the only prior art reference of record was the "Challenger No. 77" fixture.

6. More than one year prior to the filing of the application for United States Letters Patent D-138,990, there were published and known in the United States, fluorescent lighting fixtures of the same general appearance including step-down end portions, inclined side panels and louvered bottom as shown by the patents, publications, drawings and photographs embraced by defendant's Exhibits G, I and L. Inclined sides perform the function of distributing lighting outwardly and downwardly while step-down ends perform the function of allowing light to pass upwardly and outwardly against the ceiling. Louvers in the bottom perform the function of preventing glare due to direct observation of fluorescent tubes. It was common practice in the prior art to use elements connecting upper and lower rails of side panels of a lighting fixture. Length of fixtures was appropriate to the length of fluorescent tube to be employed.

7. Fluorescent light fixtures have common characteristics by reason of the utilitarian impulse. The evidence shows that lighting fixtures are largely sold to engineers, architects and builders on specifications and efficiency in the distribution of light by such fixtures, and ease of operating maintenance.

8. Plaintiff has manufactured and sold and is manufacturing and selling a fluorescent lighting fixture under the name "Viz-Aid" (exemplified by plaintiff's Exhibit 13), said fixture allegedly embodying the designs of Letters Patent No. D-138,990 and No. D-143,641. Plaintiff's "Viz-Aid" fixture does not include a V-shaped longitudinal louver having a hollow longitudinal bottom bead of circular cross-section as shown in the drawings of patent No. D-143,641; the "Viz-Aid" fixture does not embody a boss in the protruding upper end portion shown in patent No. D-138,990; the "Viz-Aid" fixture embodies the construction described in patent No. 2,411,952 (plaintiff's Exhibit 5).

9. Defendant, Ruby Lighting Corporation, has been engaged in the business of manufacturing lighting fixtures in Los Angeles since 1942; its president, Ben Ruby, has been in the lighting fixture business since 1927. Plaintiff contends that fixtures manufactured and sold by defendant under the name "Paramount," and exemplified by plaintiff's Exhibits 14 and 15, infringe the Letters Patent in suit and that defendant has performed acts of unfair competition in connection with the manufacture and sale of said fixtures.



10. Defendant's fixtures, exemplified by plaintiff's Exhibits 14 and 15, do not employ a V-shaped longitudinally extending louver having a hollow longitudinal bottom bead of circular cross-section of the character shown in Letters Patent No. D-143,641. Defendant does not use specular metal on the longitudinal louvers of its "Paramount" fixtures, Exhibits 14 and 15.

11. Defendant does not use, in its "Paramount" fixtures exemplified by Exhibits 14 and 15, a zigzag design such as is shown in Letters Patent No. D-138,990; an entirely different design or ornamentation is used by defendant on its accused fixtures. Each of the step-down ends of defendant's fixtures are single castings which do not include a protruding upper portion. [31] Defendant's fixtures do not employ the construction of plaintiff's fixtures and the louvered bottom is manipulated in a totally different manner. Defendant's fixtures, exemplified by Exhibits 14 and 15, employ forms and proportions which are common to lighting fixtures as a class and illustrated in prior art fixtures, and do not involve inventive change over the prior art.

12. The evidence does not establish that the purchasing public recognizes plaintiff's fluorescent fixtures as plaintiff's products by reason of the appearance of plaintiff's products. The evidence does not establish that plaintiff's lighting fixtures embody non-functional distinctive elements of appearance which are associated with the purchasing public with plaintiff as the source. There is no evidence

that the form of "Viz-Aid" fixtures is associated in the minds of prospective customers or purchasers with plaintiff as the source. The evidence does not establish secondary meaning in the appearance or form of fixtures so sold by plaintiff.

13. Plaintiff has not proven and established that defendant has sold and palmed off upon the purchasing public, a lighting fixture or fixtures made by defendant as and for plaintiff's fixture or fixtures. There is no evidence that defendant has misrepresented its products as those of plaintiff.

14. Defendant has not copied non-functional, ornamental and distinctive elements of design from plaintiff.

#### Conclusions of Law

1. This Court has jurisdiction of the parties and of the subject matter.

2. Title in United States Letters Patent No. D-138,990 and No. D-143,641 is vested in plaintiff, Day-Brite Lighting, Inc.

3. If valid, United States Letters Patent No. D-138,990 is limited to a design including an end plate provided with [32] specific zigzag ornamentation in its lower portion, as illustrated in the drawings of said Letters Patent.

4. If valid, United States Letters Patent No. D-143,641 is limited to a design including a longitudinal V-shaped louver having a hollow longitudinal bottom bead of circular cross-section, as

illustrated in the drawings of said Letters Patent.

5. Defendant, Ruby Lighting Corporation, has not infringed United States Letters Patent No. D-138,990 by the manufacture and sale of fluorescent lighting fixtures exemplified by Exhibits 14 and 15.

6. Defendant, Ruby Lighting Corporation, has not infringed Letters Patent No. D-143,641 by the manufacture and sale of fluorescent lighting fixtures exemplified by Exhibits 14 and 15.

7. Defendant, Ruby Lighting Corporation, has not performed acts of unfair competition as alleged in the first amendment to the complaint herein.

8. The complaint will be dismissed on the merits, with the judgment and decree in conformity to the findings and conclusions, with costs and attorneys' fees to defendant.

Dated this 12th day of April, 1950.

/s/ JAMES M. CARTER,

Judge, U. S. District Court.

Receipt of copy acknowledged.

Lodged March 30, 1950.

[Endorsed]: Filed April 12, 1950. [33]

In the United States District Court, Southern District of California, Central Division

Civil Action No. 8381-C

DAY-BRITE LIGHTING, INC., a Corporation,  
Plaintiff,

vs.

RUBY LIGHTING CORPORATION, a Corporation,  
Defendant.

JUDGMENT AND DECREE DISMISSING  
COMPLAINT AND FIRST AMENDMENT  
THERE TO ON THE MERITS WITH  
COSTS & ATTORNEYS' FEES TO DEFENDANT

This cause having come on for trial and having been heard February 28, 1950, March 1, 2 and 3, 1950, upon the pleadings and proofs, briefs and memoranda having been filed, and oral arguments being had, and the Court being fully advised in the premises; now, therefore, upon consideration thereof and upon the findings of fact and conclusions of law filed concurrently herewith,

It Is Hereby Ordered, Adjudged and Decreed by the Court as Follows:

1. The Court has jurisdiction of the parties and of the subject matter. [35]

2. Letters Patent No. D-138,990, assigned to plaintiff Day-Brite Lighting, Inc., a corporation, if valid, is limited to the specific zigzag design in the



lower portion of the end of a fluorescent lighting fixture, as shown in the drawings forming a part of said Letters Patent.

3. Letters Patent No. D-143,641, assigned to plaintiff Day-Brite Lighting, Inc., a corporation, if valid, is limited to the specific longitudinally extending V-shaped louver provided with a longitudinal bottom bead of circular cross-section shown in the drawings of said Letters Patent.

4. Defendant Ruby Lighting Corporation has not infringed Letters Patent No. D-138,990 and No. D-143,641, or either of them, if said Letters Patent or either of them are valid.

5. Defendant Ruby Lighting Corporation has not performed and is not guilty of acts of unfair competition.

6. The complaint and first amendment to the complaint are dismissed with prejudice. Defendant shall recover from plaintiff its costs of suit and disbursements, including reporter's fees and attorneys' fees in the sum of \$3,000.00. Costs taxed in the sum of \$388.99.

Dated this 12th day of April, 1950.

/s/ JAMES M. CARTER,

United States District Judge.

Judgment entered April 12, 1950.

Receipt of copy acknowledged.

Lodged March 30, 1950.

[Endorsed]: Filed April 12, 1950. [36]

[Title of District Court and Cause.]

### NOTICE OF APPEAL

Notice is hereby given that Day-Brite Lighting, Inc., Plaintiff herein, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the judgment and decree entered in this action on April 12, 1950.

Dated: At Los Angeles, California, this 9th day of May, 1950.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.

HARRIS, KIECH, FOSTER &  
HARRIS,

WARD D. FOSTER,  
JACK BARRY, JR.,

By /s/ WARD D. FOSTER,  
Attorneys for Plaintiff.

[Endorsed]: Filed May 10, 1950. [38]

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[Title of District Court and Cause.]

### COST AND SUPERSEDEAS BOND ON APPEAL

Know All Men by These Presents,

That Massachusetts Bonding and Insurance Company, a corporation organized and existing under the laws of the State of Massachusetts, and duly licensed to transact business in the State of California, is held and firmly bound under the Defendant in the above-entitled suit in the penal sum of Two

Hundred Fifty & No/100 Dollars (\$250.00), and the sum of Three Thousand Six Hundred Twenty-Seven and 29/100 Dollars (\$3,627.29) (totalling Three Thousand Eight Hundred Seventy-Seven and 29/100 Dollars = \$3,877.29) to be paid to said Defendant, its successors and assigns, for which payment will and truly to be made, the Massachusetts Bonding and Insurance Company binds itself, its successors and assigns firmly by these presents.

Sealed with our seals and Dated this 19th day of May, A.D. 1950.

The Condition of the above obligation is such that Whereas the said Plaintiff, Day-Brite Lighting, Inc., is about to take an appeal to the United States Court of Appeals for the Ninth Circuit to reverse a judgment and decree made, rendered, and entered on the 12th day of April, 1950, by the United States District Court for the Southern District of California, Central Division, in the above-entitled cause, which judgment provided that Ruby Lighting Corporation, Defendant, should recover from Day-Brite Lighting, Inc., Plaintiff, attorneys' fees in the sum of Three Thousand & No/100 Dollars (\$3,000.00) and costs taxed in the sum of Three Hundred Eighty-nine and 99/100 Dollars (\$389.99). [39]

Now Therefore, the condition of the above obligation is such that, if Day-Brite Lighting, Inc., Plaintiff, shall prosecute its said appeal to effect, and if it satisfy said judgment together with costs, interest, and damages for delay if for any reason the appeal is dismissed or if the judgment is affirmed, and if it satisfy in full such modification

of the judgment and such costs, interest, and damages as the Appellate Court may adjudge and award, then this obligation shall be void; otherwise to remain in full force and effect.

MASSACHUSETTS BONDING AND INSURANCE COMPANY.

[Seal] By /s/ WALKER B. SEABORN,  
Attorney-in-Fact.

Examined and Recommended for Approval as  
Provided in Rule 8.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.

HARRIS, KIECH, FOSTER &  
HARRIS,  
WARD D. FOSTER,  
JACK BARRY, JR.,

By /s/ WARD D. FOSTER,  
Attorneys for Plaintiff.

I hereby approve the foregoing bond.

Dated: At Los Angeles, California, this 26th day  
of May, 1950.

/s/ JAMES M. CARTER,  
Judge.



State of California,  
County of Los Angeles—ss.

On this 19th day of May in the year one thousand nine hundred and 50, before me Catharine V. Wilson, a Notary Public in and for the said County and State, residing therein, duly commissioned and sworn, personally appeared Walker B. Seaborn, known to me to be the duly authorized Agent and Attorney-in-Fact of the Massachusetts Bonding and Insurance Company, the corporation whose name is affixed to the foregoing instrument; and duly acknowledged to me that he subscribed the name of the Massachusetts Bonding and Insurance Company thereto as Surety and his own name as Attorney-in-Fact.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Seal]      /s/ CATHARINE V. WILSON,  
Notary Public in and for Said  
County and State.

[Endorsed]: Filed May 26, 1950.

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[Title of District Court and Cause.]

ORDER STAYING JUDGMENT FOR AT-  
TORNEYS' FEES AND TAXED COSTS

Plaintiff by its counsel having applied to this Court for a writ of supersedeas to stay the judg-

ment that Defendant shall recover from Plaintiff attorneys' fees in the sum of Three Thousand Dollars (\$3,000.00) and costs taxed in the sum of Three Hundred Eighty-nine and Ninety-nine/100 Dollars (\$389.99), entered in this action on April 12, 1950, pending the appeal of said Plaintiff from said judgment; and the Court being fully advised in the premises, in consideration thereof;

It Is Hereby Ordered and Decreed:

That the said judgment for the payment by Plaintiff to Defendant of attorneys' fees in the sum of Three Thousand Dollars (\$3000.00) and of costs taxed in the sum of Three Hundred Eighty-nine and Ninety-nine/100 Dollars (\$389.99) be, and it hereby is, [41] suspended and stayed pending the determination of said appeal or until order of Court upon the condition that the Plaintiff file herein with the Clerk of this Court, on or before May 26, 1950, a good and sufficient bond in the sum of Three Thousand Six Hundred Twenty-seven and Twenty-nine/100 Dollars (\$3,627.29) (in addition to the Two Hundred Fifty Dollar [\$250.00] cost bond on appeal) conditioned for the satisfaction of said judgment together with costs, interest, and damages for delay if for any reason the appeal is dismissed or if the judgment is affirmed and to satisfy in full such modification of the judgment and such costs, interest, and damages as the Appellate Court may adjudge and award; the Court reserving the right to increase the amount of the supersedeas bond for sufficient cause shown.

Dated: At Los Angeles, California, this 26th day of May, 1950.

/s/ JAMES M. CARTER,  
Judge.

The foregoing order is consented to and approved as to form, this 16th day of May, 1950.

C. A. MIKETTA,  
WILLIAM W. GLENNY,

By /s/ C. A. MIKETTA,  
Attorneys for Defendant.

[Endorsed]: Filed May 26, 1950. [42]

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[Title of District Court and Cause.]

STIPULATION AND ORDER RE EXTENSION  
OF TIME FOR FILING RECORD ON AP-  
PEAL AND DOCKETING APPEAL

It Is Hereby Stipulated, by and between the parties to the above-entitled cause, through their respective counsel and subject to the approval of the Court, that the time within which the record on appeal may be filed and the appeal docketed in the Court of Appeals may be extended to and including August 8, 1950.

Dated: At Los Angeles, California, this 5th day of June, 1950.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.

HARRIS, KIECH, FOSTER &  
HARRIS,

WARD D. FOSTER,  
JACK BARRY, JR.,  
By /s/ WARD D. FOSTER,  
Attorneys for Plaintiff.

C. A. MIKETTA,  
WM. W. GLENNY,  
By /s/ C. A. MIKETTA,  
Attorneys for Defendant.

Approved and It Is So Ordered, this 7th day of  
June, 1950.

/s/ PAUL J. McCORMICK,  
Judge.

[Endorsed]: Filed June 7, 1950. [43]

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[Title of District Court and Cause.]

CONCISE STATEMENT OF PLAINTIFF-AP-  
PELLANT'S POINTS ON APPEAL PUR-  
SUANT TO F.R.C.P. 75(d)

Now comes the Plaintiff-Appellant, Day-Brite Lighting, Inc., and, in accordance with Rule 75(d) of the Federal Rules of Civil Procedure, makes the following concise statement of points on which it intends to rely for appeal to the United States Court of Appeals for the Ninth Circuit from the final judgment made and entered April 12, 1950, in this cause:

(1) The Court erred in holding that United States Letters Patent No. D-138,990 are limited to the specific zigzag design in the lower portion of



the end of a lighting fixture as shown in the drawings forming a part of said Letters Patent and in failing to hold that said Letters Patent are valid as covering the ornamental design for a louvered fluorescent lighting fixture as shown and described in said Letters Patent. [44]

(2) The Court erred in holding that United States Letters Patent No. D-143,641 are limited to the specific longitudinally extending V-shaped louver provided with a longitudinal bottom bead of circular cross-section shown in the drawings of said Letters Patent and in failing to hold that said Letters Patent are valid as covering the ornamental design for a louvered fluorescent lighting fixture as shown and described in said Letters Patent.

(3) The Court erred in holding that Defendant, Ruby Lighting Corporation, has not infringed United States Letters Patent No. D-138,990 and erred in failing to hold that Defendant has infringed said Letters Patent.

(4) The Court erred in holding that Defendant, Ruby Lighting Corporation, has not infringed United States Letters Patent No. D-143,641 and erred in failing to hold that Defendant has infringed said Letters Patent.

(5) The Court erred in holding that Defendant, Ruby Lighting Corporation, had not performed and was not guilty of acts of unfair competition and in failing to hold that Defendant had performed and

was guilty of acts of unfair competition with Plaintiff.

(6) The Court erred in failing to hold that Plaintiff, Day-Brite Lighting, Inc., by the expenditure of much effort and money, over a long period of time, in advertising and acquainting the trade and purchasing public with fluorescent lighting fixtures subject of the patents in suit and manufactured by it, and by the extensive sales of such fluorescent lighting fixtures to the trade and public, has created a market and demand for said fluorescent lighting fixtures of Plaintiff's manufacture and a recognition by the trade and public of said fluorescent lighting fixtures and their merit and dependability by their appearance, and a recognition by the trade and public of the distinctive [45] appearance of said fluorescent lighting fixtures and the non-functional ornamental attributes thereof and the secondary significance and meaning of such distinctive appearance and attributes, as indicating origin in and manufacture by Plaintiff, and in failing to hold that Defendant, Ruby Lighting Corporation, by its manufacture and sale of fluorescent lighting fixtures having said distinctive appearance and said attributes thereof, has appropriated the market and demand of the trade and public for Plaintiff's said fluorescent lighting fixtures and has caused confusion in the minds of the trade and public between the fluorescent lighting fixtures of Plaintiff and those of Defendant and has competed unfairly with Plaintiff.

(7) The Court erred in holding that Defendant,

Ruby Lighting Corporation, should recover from Plaintiff, Day-Brite Lighting, Inc., its attorneys' fees in the sum of Three Thousand Dollars (\$3,000.00), or any other sum, and its taxable costs and disbursements, and in failing to hold that Plaintiff should recover from Defendant reasonable attorneys' fees and its taxable costs and disbursements.

Dated: At Los Angeles, California, this 29th day of June, 1950.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.

HARRIS, KIECH, FOSTER &  
HARRIS,

WARD D. FOSTER,  
JACK BARRY, JR.,

By /s/ WARD D. FOSTER,  
Attorneys for Plaintiff.

Receipt of copy acknowledged.

[Endorsed]: Filed June 30, 1950. [46]

In the District Court of the United States for the  
Southern District of California, Central Division

No. 8381-C Civil

DAY-BRITE LIGHTING, INC., a Corporation,  
Plaintiff,

vs.

RUBY LIGHTING CORPORATION, a Corpora-  
tion,

Defendant.

Honorable James M. Carter, Judge Presiding

REPORTER'S TRANSCRIPT OF  
PROCEEDINGS

Tuesday, February 28, 1950

Appearances:

For the Plaintiff:

HARRIS KIECH, FOSTER & HARRIS, By  
WARD D. FOSTER, ESQ., and  
JACK BARRY, JR., ESQ.,  
417 South Hill Street,  
Los Angeles 13, California, and  
CARR & CARR & GRAVELEY,  
Of Counsel.

For the Defendant:

CASIMIR A. MIKETTA, ESQ.,  
WILLIAM W. GLENNY, ESQ., and  
KNIGHT, GITELSON & ASHTON,  
Of Counsel.



I wish at this time, your Honor, to offer in evidence a copy certified by the United States Patent Office of the file wrapper and contents of patent in suit No. 138,990, as Plaintiff's Exhibit 3, and a similar certified copy of the other design patent in suit, No. 143,641, as Plaintiff's Exhibit 4. They bear upon the back a notary's reference to an exhibit number, because they were used in depositions.

The Court: These are the file wrappers?

Mr. Foster: Those are the file wrappers and contents, your Honor.

The Court: They will be received into evidence as Plaintiff's 3 and 4. [25\*]

\* \* \*

At the same time, your Honor, and pursuant to the stipulation, I will offer the Biller patent 2,411,952 as Plaintiff's Exhibit 5.

The Clerk: Are you offering it in evidence?

Mr. Foster: Yes.

The Court: It will be received in evidence.

(The document referred to was marked Plaintiff's Exhibit No. 5 and was received in evidence.)

Mr. Foster: That is the same Mr. Biller who has one of the design patents in suit.

The Court: This is a mechanical patent?

Mr. Foster: Yes. I wanted to show your Honor that in an attempt by this patent law firm in St. Louis to provide all possible assurance that their investment was justified in this new fixture for the

plaintiff, they applied for a mechanical patent upon  
sofe of the machanical elements of this fixture.

\* \* \* But all that was new mechanically in this  
fixture, as contrasted with design, was the specific  
combination of specific elements and the manner in  
which they mechanically interlocked and were as-  
sembled. [27]

\* \* \*

Mr. Foster: I now offer the volume of prior  
patents marked Exhibit 10, for identification, as  
our exhibit of the same number. [35]

The Court: Any objection?

Mr. Miketta: The only objection I shall make  
is that the heading of Plaintiff's Exhibit 10, for  
identification, be changed. "Prior Art Designs" is  
perfectly all right, but the words "Defendant May  
Have Copied Without Infringement" is a conclu-  
sion, and I think should not appear on this exhibit.

\* \* \*

The Court: Let's strike out on Exhibit 10 every-  
thing other than "Prior Art Designs."

\* \* \*

The Court: No. 10, therefore, will be received  
in evidence. [36]

(Thereupon the document heretofore marked  
Plaintiff's Exhibit 10 was received in evidence  
and the "Table of Contents" thereof is in the  
words and figures as follows, to wit:)

Table of Contents

A—1,293,594—Willey
B—2,339,010—Greenwald
C—2,364,992—Maurette
D—D-112,634—Devol
E—D-119,794—Robinson
F—D-119,810—Segil
G—D-120,913—Hirsh
H—D-122,145—MacCarthy
I—D-122,156—Biller
J—D-122,581—Arakelian
K—D-122,582—Biller
L—D-122,694—Rubinstein
M—D-122,709—Korengold
N—D-122,861—Carter
O—D-122,887—Beals
P—D-122,909—Stern
Q—D-123,048—Doane
R—D-123,049—Doane
S—D-123,067—Rubinstein
T—D-124,527—Dreyfuss
U—D-124,888—Callahan
V—D-125,091—Miles [37]

W—D-127,596—Walsh

X—D-127,685—MacCarthy

Y—D-127,823—Biller

Z—D-127,914—Scribner

AA—D-128,478—Carter

AB—D-128,968—Scribner

AC—D-129,726—Scribner

AD—D-130,256—Scribner

AE—D-130,449—Weber

AF—D-130,656—Carter

AG—D-130,745—Mausshardt

AH—D-130,809—Waltman

AI—D-130,810—Baker

AJ—D-131,199—Mitchell

AK—D-131,478—Koegel

AL—D-131,532—Naysmith

AM—D-131,845—Biller

AN—D-132,786—Netting

AO—D-133,214—Ohm

AP—D-133,216—Parlato

AQ—D-133,986—Gordon

AR—D-134,079—Gordon

AS—D-134,080—Gordon



AT—D-134,081—Gordon

AU—D-136,453—Masterson

AV—D-136,797—Mareck [38]

Mr. Foster: Under the same stipulation, I offer the volume marked “Prior Art Designs From Catalogs” as Plaintiff’s Exhibit 9.

The Court: We will strike everything after the word “Catalogs,” so that it will read “Prior Art Designs From Catalogs,” and No. 9 will be received in evidence.

(Thereupon the volume heretofore marked Plaintiff’s Exhibit 9 was received in evidence and the “Table of Contents” thereof is in the words and figures as follows, to wit:)

#### Table of Contents

A—1941 Ruby Catalog “Fluorescent Lighting”

B—Illuminating Engineering, Vol. XXXVI, No. 2 (Feb., 1941)

C—Illuminating Engineering, Sept., 1942, and particularly pages 466 and 472

D—Illuminating Engineering, March, 1943, and particularly pages 130 and 131

E—Illuminating Engineering, April, 1943, and particularly pages 168 and 169

F—Catalog No. 38 of The Edwin F. Guth Co. (March 1, 1941) and particularly pages 7, 18, 19 and 23

G—The Magazine of Light, No. 9 issue, 1940, article entitled “A Review of Fluorescent Luminaire Design”

H—Garcy Challenger [39]

Mr. Foster: Now I have an oral stipulation, your Honor, covering the Plaintiff’s patented design which is upon the standard here, and which when your Honor opened court this morning was lighted. That design is suspended from the standard because we hope that to an observer seated on the floor of the court room it would approach in location a fixture hinged to or suspended a short distance below the ceiling. Of course, to your Honor on the bench it does not have that appearance because the bench is elevated. But that fixture, which is of plaintiff’s manufacture, has been seen by defendant’s counsel, and we offer it in evidence as the commercial embodiment of the plaintiff’s patented design as plaintiff’s next in number.

The Court: Plaintiff’s Exhibit 13. It will be received in evidence.

\* \* \*

Mr. Foster: We have two fixtures of the defendant’s manufacture, one of them given to us by the defendant, and I offer as Plaintiff’s Exhibit 14 the smaller of those two accused fixtures. [40]

\* \* \*

Mr. Foster: The smaller one is offered as Plaintiff’s Exhibit 14. There are two sizes, your Honor,

because one of them takes two fluorescent tubes, and one of them takes four for a greater degree of light.

Mr. Miketta: The defendant will stipulate that both of these fixtures are of its manufacture, your Honor.

Mr. Foster: And were sold, Mr. Miketta, in the Southern District of California, Central Division, prior to the filing of the complaint, for jurisdictional reasons?

Mr. Miketta: That that is the same type of fixture that was sold?

Mr. Foster: Yes.

Mr. Miketta: So stipulated.

\* \* \*

The Court: 14 will be the smaller. And the larger one?

Mr. Foster: The larger one as Plaintiff's Exhibit 15.

The Court: They will be received in evidence pursuant to the stipulation of counsel. [41]

\* \* \*

Los Angeles, California

Tuesday, February 28, 1950, 2:30 P.M.

The Court: Proceed.

\* \* \*

Mr. Foster: And may the record show that we have had a lamp up here on the stand all morning from 10:00 to 11:40, and lighted for about the first five or ten minutes. I wanted to ask the permission

of the court to move it during the afternoon. Your Honor saw it this morning, and saw it lighted. Can you see a little of the end plate from up there?

The Court: Where are you going to move it to?

Mr. Foster: I am going to move it out of the way for witnesses to go back and forth.

Can you see a little of the end plate, your Honor? [54]

The Court: Yes, I can see a little bit. Do you want to turn the light on again?

Mr. Foster: No. I just wanted you to see it there.

I notice that the clerk has tagged it. It is about 20 feet from the judge's bench, perhaps, and 15 feet from the clerk. You have tagged this as Plaintiff's Exhibit 13 as the plaintiff's lamp. Is that correct, Mr. Clerk?

The Clerk: Yes.

Mr. Foster: May the record show that the clerk has been here all during the morning session? He did not know that the lamp now on the standard is not the plaintiff's lamp, but has so labeled it, although it is the defendant's lamp.

Had your Honor noticed that difference? Does your Honor notice that this is a different lamp than the one this morning? Your Honor hadn't remarked about it, and it is perhaps an unfair question. But I assure your Honor that I was not in cahoots with the clerk in having it marked this way.

The Court: You mean you are not referring to the standard or to the ceiling plate, but that the



lamp is a different one than was up there this morning?

Mr. Foster: Yes, your Honor. Does that surprise you?

I think it fair to state for the record that the clerk did not observe any difference although he was two hours in [55] court this morning, and of his own volition and at no suggestion from plaintiff's counsel he has seen fit to label this lamp Plaintiff's Exhibit 13 when he came in at 2:00 o'clock, whereas Plaintiff's Exhibit 13 is over there on the bench, and the exhibit up here on the standard which he sought to label is Plaintiff's Exhibit No.—

The Court: 14 or 15?

Mr. Foster: 14, which is the defendant's lamp.

The Clerk: You just removed the top of the standard?

Mr. Foster: Yes. And, of course, at the appropriate time I will urge that the appropriate test of infringement is that of the casual observer, and that as the casual observer the clerk observed the lamp this morning for two hours and couldn't tell the difference.

The Clerk: Should that tag be removed from the standard and put on the lamp over there?

Mr. Foster: Yes, sir.

The Court: You don't have to do it now, Mr. Clerk.

The Clerk: All right.

Mr. Miketta: I am quite sure that the change of the lamp was completely inadvertent.

Mr. Foster: No. We intended to change them,

but we didn't plan with the clerk that he would mark them erroneously. [56]

\* \* \*

Mr. Miketta: Now, I believe plaintiff will stipulate that they did not invent the fluorescent tube.

Is that correct, Mr. Foster?

Mr. Foster: Yes. [60]

\* \* \*

### BERTRAM A. KAEPPPEL

called as a witness by and on behalf of the plaintiff, having been first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Foster:

Q. Will you state your full name, please, Mr. Kaepffel.

A. Bertram A. Kaepffel, K-a-e-p-p-e-l. [70]

Q. And your age, please, Mr. Kaepffel?

A. My age is 42.

Q. And your residence?

A. 5354 Delmar Avenue.

Q. What city?

A. St. Louis, Missouri.

Q. You are the Mr. Kaepffel who was one of the patentees named in each of the design patents here in suit?

A. Yes, I am.

Q. You are employed by Day-Brite Company, the plaintiff here?

A. Yes.

Q. Did you have any experience prior to your

(Testimony of Bertram A. Kaepfel.)

employment by the plaintiff in designing any appliances or apparatus?

A. Yes, sir. Shall I enumerate them?

Q. If your please.

A. From 1924 to 1928 I worked for the Busch Sulzer Brothers Diesel Engine Company as a draftsman.

\* \* \*

A. (Continuing): In the year following that, for the American Cotton Picker Company. Do you want me to go on [71] from there?

Q. (By Mr. Foster): Yes.

A. For four years following that I was on a farm, and then two years out of work due to ill health.

Q. How long have you been with the Day-Brite Lighting, Inc.?

A. From October 21, 1935, continuously.

Q. All of your work for the Day-Brite Lighting, Inc., has been in their engineering department, is that correct?

A. Yes, sir.

Q. Your work now is that of a tool engineer and designer, is that true?

A. Yes, sir.

Q. Have you participated in the making of any inventions other than those of the two patents here in suit, Mr. Kaepfel?

A. I have participated in others where patent has been applied for but not as yet granted.

Q. The two patents in suit represent the only inventions you have participated in where a patent has been issued, is that correct?

A. Yes, sir.

(Testimony of Bertram A. Kaepfel.)

Q. Approximately when was the commencement of your work on making the designs of the two patents in suit?

A. That would have been prior to February, 1943, to [72] the best of my memory.

Q. What was the original purpose that you had in mind when you commenced work upon this design?

A. The original purpose would have been to produce a fixture which would be readily stockable on the part of all distributors and dealers, it would be readily producible in the shop, and would have the pleasing appearance that would make it salable.

Q. Now, those purposes of having a fixture that would be readily stocked and readily produced in the shop are purposes had in mind in the manufacture of all commercial devices to be sold, isn't that true, within your experience?      A. Yes, it is.

Q. But you had as a purpose here, also, in making the designs of the patent in suit, providing a fixture that was of a pleasing eye appeal so that it would be sold, if I understand you, is that right?

A. Yes, that is of primary importance. A fixture that is not appealing to the eye will not sell.

Q. Was your purpose in working upon the design of the fixtures of the patents in suit to provide such a pleasing appearance to the fixture that it would become a best seller with the company? [73]

\* \* \*



(Testimony of Bertram A. Kaepfel.)

The Witness: The plain answer is yes, it was. [74]

\* \* \*

Q. (By Mr. Foster): In your work upon the design of the two patents in suit, were any sketches or drawings of fixture [75] designs made?

A. Yes, there would be very many sketches made.

Q. Did you have anything to do with making those sketches or drawings in the development of the designs of the patents in suit?

A. Yes, sir, I made them personally.

Q. You say a great many. How many were made, if any, before the final design of the patents in suit was reached?

A. That is a difficult question to answer because many of these sketches would be destroyed as we progressed in our design. I would say certainly several dozen.

Q. Is my understanding correct that as the sketch of a design was superseded by a subsequent one, those superseded sketches were not always retained? Is that true? A. That is true.

Q. Have you made an examination of the company files to search for sketches of those preliminary designs which might have happened to be retained?

A. Yes, sir, I believe the first one is dated May, 1943.

Q. I show you a copy of Plaintiff's Exhibit 1, containing five drawings tabbed A to E; are those

(Testimony of Bertram A. Kaepfel.)

the drawings which you found as a result of that search?      A. Yes, sir.

Q. That is Plaintiff's Exhibit 1, for identification. [76] Would you carefully examine each of the five drawings in Plaintiff's Exhibit 1 for identification and state who made the originals of those drawings?

A. Yes, sir; I made every one of them.

Q. When were those drawings tabbed A to E inclusive of Plaintiff's Exhibit 1 for identification made by you with respect to the dates which they bear?

A. They would have been made within a few days prior to the date on the drawing.

Q. The date appearing upon each of these five drawings in Plaintiff's Exhibit 1, for identification, is in your hand?      A. Yes, sir.

Q. It was your custom, as I understand you, to date these drawings so made by you at or within a day or two after your completion of the drawing, is that correct?      A. That is correct.

Q. And have the originals of these drawings A to E of Plaintiff's Exhibit 1, for identification, been in the files of Day-Brite in the engineering department since they were made until removed for printing by you?

A. Yes, sir, since that date. [77]

\* \* \*

Q. (By Mr. Foster): And have any changes or additions been made in these drawings since the dates which they bear respectively?

(Testimony of Bertram A. Kaepfel.)

A. No, sir, there have not.

Q. Will you refer briefly to these drawings successively and give us a short description of what is there contained as regards the finished design of the patents in suit? [78] Refer first to the drawing which is dated 5-20-43, tab A of Plaintiff's Exhibit 1, for identification.

A. The drawing dated 5-20-43 is a free-hand cross-section through the chassis of the fixture. It shows the ballast and the lamp holder sketched in place with a suggestion for joining the two components.

Q. Would you refer to tab B, the next drawing, dated 3-28-44, and describe what is there generally disclosed?

A. That drawing shows, perhaps, the first concrete suggestion for a completed fixture. It indicates the elements of the design as they were taking shape at that time.

Q. I note that in the center of tab B of Plaintiff's Exhibit 1, for identification, there is in the right-hand side of the center view a representation that appears to be part of the end plate, is that correct?

A. Yes, sir.

Q. And I notice that in the lower portion of the right-hand half of the center view there appears to be an ornamentation of the end cap or plate, is that correct?

A. Yes, sir, that is the way it was originally conceived.

Q. But I notice that ornamentation in the lower

(Testimony of Bertram A. Kaepfel.)

right half of the central view of tab B does not have an outline around it tying it to the ornamentation on the other half. Was that conceived of at that time? [79]

A. Not at the time that this drawing was made. That followed later.

Q. And this drawing was made 3-28-44?

A. Yes, sir.

Q. I note on the right-hand edge of tab B of this drawing a representation. What is there shown? Is that the side section of the fixture?

A. That is what is known as an elevation at the center of the fixture indicated by a broken line separating the end from the center.

Q. Then this vertical line is the center of the side of the fixture, is that correct?

A. Yes, that is the center.

Q. And does that view on the right of tab B drawing of Plaintiff's Exhibit 1, for identification, indicate that there was to be centrally disposed on each side of the fixture three rectangular panels?

A. Yes, sir.

Q. Decorative panels. Is there any indication on tab B of the spacing of the louvers, transverse louvers?

A. Yes, at the left-hand side of the drawing there is an indication of the number of transverse louvers to be applied throughout the fixture.

Q. Does this left-hand view of tab B illustrate to scale how far apart the transverse louvers are spaced? [80]



(Testimony of Bertram A. Kaepfel.)

A. Yes, by scaling the original drawing we knew exactly what that dimension was to become.

Q. And there is indicated in the left-hand view the overall length of the fixture?

A. Yes, sir.

Q. So that from the scale distance of the transverse louvers shown on tab B and the overall length you knew there were how many transverse louvers to be there?

A. Yes, we knew there would be 13 transverse louvers.

\* \* \*

Q. (By Mr. Foster): Will you, Mr. Kaepfel, refer to the drawing? In the lower left I notice a dimension line 48-7/16 inches. Is that the overall length of the louver?

A. That was the overall length of the fixture. And then by scaling this drawing we knew exactly what that spacing would become.

The Court: I know, but is there anything on this drawing to show that there couldn't have been 15 louvers or 20 louvers? [81]

The Witness: Yes, sir. The distance from the end to the first louver, or the first louver to the second louver, would have been——

The Court: Where is the distance from the end of the first louver shown?

The Witness: The transverse louver is indicated by the long shaded vertical line.

The Court: The first louver?

(Testimony of Bertram A. Kaepfel.)

The Witness: Yes, that is the first transverse louver.

The Court: You show no distance of that louver from the end?

The Witness: That's right. The dimension was not put in there at that time because this was a discussional drawing and a drawing for making up a sample to be mounted and viewed and criticized.

Mr. Foster: But it is a scale drawing, is it?

The Witness: It is drawn to scale. [82]

\* \* \*

Q. (By Mr. Foster): Will you refer to drawing tab C of Plaintiff's Exhibit 1, for identification, dated 5-18-44, and describe briefly what is there disclosed?

A. The drawing 5-18-44 shows another step in the development of this design. By this time we have reached the thought of a V-shape central longitudinal louver, we have unified the design in the end of the fixture, we have altered the end cover and have pretty well stabilized the contours or outline of the fixture.

Q. Mr. Kaepfel, the record will not show where you have pointed. When you say that you have unified the design in the end cap, by that do you mean that you have placed around the decorative pattern in each of the lower halves of the end cap an outline which contains them both? [83]

A. Yes, sir, that is correct.

Q. As shown in this drawing?

A. Yes.

\* \* \*

(Testimony of Bertram A. Kaepfel.)

Q. (By Mr. Foster): When you say that you have reached a central triangular configuration, you are pointing to the one half of the triangle in the lower center right-hand side of the central view?

The Court: Shown by the letter C?

Q. (By Mr. Foster): Shown by the letter C, that is the V-shaped longitudinal louver?

A. Yes, sir.

Q. And the upper part of the end plate you are referring to is shown in the right-hand half of the central view?

A. That is correct.

Q. Would you describe briefly what is shown in the next drawing, tab E of Plaintiff's Exhibit 1, for identification, dated 7-3-45? [84]

\* \* \*

Q. 6-22-44 is the date of Exhibit D.

The Court: This looks like 6-23 to me. You have got one date written in pencil above—pardon me. It is 6-22-44.

A. This drawing shows the final design of the enclosure. On this one everything has been stabilized and is ready for production.

Q. And the two side views on the left and right are fragmentary side elevational views of the composite fixture, is that correct?

A. Yes, sir.

Q. Referring to tab E of Plaintiff's Exhibit 1, for identification, dated 7-3-45, please describe generally what is there shown?

A. That drawing shows the same enclosure, but it is now a complete fixture by virtue of the fact

(Testimony of Bertram A. Kaepfel.)

that it is mounted on the chassis which contains all the remaining components.

Q. Does it show anywhere the central V-shaped longitudinal louver?

A. Yes, sir, it shows that longitudinal louver and shows the final profile of the transverse louvers also.

Q. That is shown in the left-hand half of the central view, is that correct? [85]

A. Yes, sir.

Q. And it shows the decorative pattern in the lower portion of the end cap that is being shown on the right-hand half of the central view?

A. Yes.

Q. And the pattern and the top of the end cap is shown in the top of the right-hand half of the central figure, is that true?

A. Yes, sir.

Q. Are any of the transverse baffles illustrated there outlined?

A. Yes, in the left-hand lower cross-section of the fixture.

Q. And the central figure? A. Yes.

The Court: Marked 7?

The Witness: 7, yes, sir.

Q. (By Mr. Foster): And is that transverse louver shown, the edge of it, anywhere in the left-hand view?

A. It is shown in one location in the left-hand view.

Q. That is the edge of the transverse louver we see there? A. Yes, sir.



(Testimony of Bertram A. Kaepfel.)

Mr. Foster: These tabs A, B, C, D, and E, which the witness has identified as being made by him and produced from the [86] files of the company are offered in evidence as Plaintiff's Exhibits 1-A to -E respectively.

The Court: They will be received into evidence as Plaintiff's Exhibit 1 with the subdivisions A to E inclusive.

(Thereupon the document marked Plaintiff's Exhibit 1-A to 1-E, for identification, was received in evidence and the "Index" thereof is, in words and figures, as follows, to wit:

("Preliminary Drawing dated 5-20-43—A

("Drawing dated 3-28-44—B

("Drawing dated 5-18-44—C

("Drawing dated 6-22-44—D

("Drawing dated 7-3-45—E.")

The Court: We will take a short recess at this time, about five minutes.

(Short recess.) [87]

\* \* \*

The Court: You do not contend that the number of hours put in would indicate the spark of genius, do you?

Mr. Foster: No, your Honor.

\* \* \*

Q. (By Mr. Foster): This first drawing, Plain-

(Testimony of Bertram A. Kaepfel.)

tiff's Exhibit 1-A, dated 5-20-43, is that the first drawing that was made in developing the designs of the patents in suit?

A. By no means. There were many drawings before that.

Q. But is this the first one you were able to find that was retained? A. Yes, sir. [88]

The Court: The first drawing there, A in Exhibit 1, that is the internal holder, is it not?

The Witness: Yes, sir. That was the chassis for the fixture.

The Court: And the rest of it comes around the outside of it?

The Witness: Yes, sir.

Q. (By Mr. Foster): Is that true likewise of the periods of time between the dates of the successive drawings, of tabs A to E in Plaintiff's Exhibit 1, that there were a number of other drawings made between them and discarded?

A. Yes, that would be true in all cases. [89]

\* \* \*

Q. (By Mr. Foster): Did Mr. Biller at Day-Brite Lighting, Inc., also meet with you during the period from this first drawing, 5-20-43, to the final drawing, 7-3-45 in Plaintiff's [90] Exhibit 1?

A. Yes, Mr. Biller and I worked very closely together. There were many discussions. Every time there would be a new scope of drawing, we would talk about it and criticize it very freely.

Q. And where did those meetings take place?

(Testimony of Bertram A. Kaepfel.)

A. In the engineering department at my drafting table.

Q. Were any of these drawings, tabs A, B, C, or D, of Plaintiff's Exhibit 1 utilized in the shop to make any models or mock-ups?

A. Yes, sir. As soon as we had a drawing that was capable of being produced in metal, we always made a sample in order to get the third dimensional aspect.

Q. Were they called mock-ups?

A. Mock-ups, yes, sir; samples or mock-ups.

Q. Was any mock-up ever made of the drawing tab A, dated 5-20-43?

A. No, sir, not of that one drawing alone.

Q. Of tab B of Plaintiff's Exhibit 1?

A. Yes, I am very sure there was a sample or mock-up of that drawing.

Q. When with respect to its date, 3-28-44?

A. The sample would probably be available to us within a month after that date.

Q. Of what other drawings, tabs C, D and E of Plaintiff's Exhibit 1, were mock-ups made?

A. Of all of them except the last drawing. By that time, why, the design was stabilized.

Q. Those mock-ups were made in the shops of Day-Brite Lighting, Inc.; is that true?

A. Yes, sir.

Q. And they were observed by you, and criticized, were they?      A. Yes, sir.

Q. That is, when they were observed, do you mean the appearances of them were observed?

(Testimony of Bertram A. Kaepfel.)

A. The fixture was mounted in a position on the ceiling where it could be freely criticized by both Mr. Biller and myself, and the other engineers.

Q. Did the discussions relate to anything other than the lighting efficiencies of these designs?

A. We never checked the lighting efficiency at that stage. At that stage we were interested only in appearances.

Q. What was done with these mock-ups, these three or four mock-ups of the designs shown in Plaintiff's Exhibit 1, after they were made?

A. The mock-ups were retained until we were completely tooled for production.

Q. I notice upon Plaintiff's Exhibit 1-C the longitudinal V-shaped louver has a circular bead shown on its lower [92] end. Was such a circular bead ever used in Day-Brite fixtures?

A. Yes, it was used originally for about a year in actual production.

Q. What was the reason for the existence of that bead on the V-shaped louver?

A. The bead came into—was used in production for fastening the ends of the fixture to the longitudinal louver by means of a thread-cutting screw through the end plates.

Q. Did that circular bead on the V-shaped longitudinal louver contribute to its appealing appearance, in your opinion?

A. No, sir.

Q. It was for utility, as I understand you?

A. Yes, sir.

Q. After it had been used for a period of time



(Testimony of Bertram A. Kaepfel.)

on the Day-Brite commercial fixtures, as I understand your testimony the circular bead was eliminated?      A. Yes, sir.

Q. Was that circular bead observable?

A. Yes, sir.

Q. When the longitudinal louver was employed, you could see it when it was used, could you?

A. Yes, sir, if you looked at it closely. [93]

\* \* \*

Q. (By Mr. Foster): I direct your attention to the drawing, tab D of Plaintiff's Exhibit 1, and, again, to the longitudinal louver, the V-shaped louver. I notice there is illustrated at its upper end a little flange. Did that, in your opinion, contribute to the pleasing design or appearance of the fixture?

A. No. That was added as a stiffening member.

Q. That was a utility feature, as I understand it?      A. Yes, sir.

Q. Was that visible when the composite fixture was assembled by an observer beneath it?

A. No, sir, that would not be visible from below.

Q. And as regards the last drawing, tab E of Plaintiff's Exhibit 1, you had reached, as I understand you, the final design as regards the angle of the parts, and the slopes, and the over-all composite ornamental appearance of the patented design; is that correct?

A. Yes, sir, that is the design as frozen.

The Court: What date did you reach that final design? [94]



(Testimony of Bertram A. Kaepfel.)

The Witness: The drawing is dated 7-3-45.

Q. (By Mr. Foster): Now, were all of the changes represented in the various forms of the design in Plaintiff's Exhibit 1 approved by both you and Mr. Biller before they were made?

A. Yes, Mr. Biller was always consulted before any changes were made.

Mr. Foster: Now, that Plaintiff's Exhibit 1, your Honor, reflects, as the witness has shown, all of the drawings we could find of the development of the design to the perfected form shown in the design patents.

I now wish to direct his attention to Plaintiff's Exhibit 2, which is the work involved in preparing to manufacture the patented design commercially.

The Court: You say Plaintiff's Exhibit 1 is all of the drawings that concerned both of the design patents?

Mr. Foster: Yes, your Honor. One of the design patents is a sub-combination of the composite shown.

The Court: Which patent was the combination patent and which was the sub?

Mr. Foster: The sub-combination patent is 143,641, the patent on the longitudinal and transverse louvered assembly, and the design patent 138,990 is upon the entire combination, in the first one.

The Court: The first one was the combination?

Mr. Foster: Yes, sir.

The Court: And the second patent was on a part of the matter?

(Testimony of Bertram A. Kaepfel.)

Mr. Foster: True, your Honor. The '641 patent, the latter issue, was filed July 28, 1944, and the '990 patent, the earlier issue, was filed July 29, 1944. I don't know why one day elapsed between them, but they were directed to the same fixture, as is shown by the fact that in the '641 later issued patent the outline is in dots or a phantom showing, which is customary in a design patent drawing to show the environment of the design, which design is not covered by the design patent.

Q. (By Mr. Foster): Now, I asked you, Mr. Kaepfel, to make a search for drawings and a search relating to work done to prepare for commercial production of the fixtures of the design patents in suit. Are these drawings which are in plaintiff's Exhibit 2, for identification, those which you found in response to that request?

A. Yes, sir. They are in that binder.

Q. And found at the beginning of this Plaintiff's Exhibit 2, for identification, is a sheet entitled, "Summary of Tool Costs viz-aid fixtures," showing a total expenditure of \$59,445.67, and followed by sheets which list those expenditures, commencing in 1944 and continuing through to 3-22-48. Were those compilations prepared by you or under your direction?

A. They were prepared by me or under my direction.

Q. They are the compilations which are summarized in this total sheet of \$59,000-plus in this exhibit?

A. Yes, sir.

(Testimony of Bertram A. Kaepfel.)

Q. From what sources did you get the material compiled in these typed sheets for that total?

A. From the invoices by our die suppliers.

Q. Those invoices, in the normal course of business, pass through your hands before they are paid?

A. Yes, sir. They come to me for approval for payment.

\* \* \*

Mr. Miketta: May the court please: I don't know what your ultimate ruling on this will be, but it seems to me that we are burdening the record and burdening the time of the court, and taking your time unnecessarily, your Honor, in talking about tool costs, where many of the tool costs, for example, as indicated by the first sheet, relate to the chassis. Now, the chassis is the tin-can that carries the socket and the tube, and has nothing to do with the design, and I am quite sure that the witness would admit that a chassis of that type has been used by other lamps. [97]

Now, the amount of money spent by them on their own tools is absolutely irrelevant and immaterial. That has nothing to do with the design. Just because they are more or less efficient in manufacturing the devices certainly does not influence either the question of validity or the question of the scope or the question of infringement.

\* \* \*

Mr. Foster: I urge, your Honor, the materiality, of course, and I propose to ask general questions

(Testimony of Bertram A. Kaepfel.)

that will cover all of them instead of going through each in detail. But I feel it is all material as indicating that when one does, as did the plaintiff here, independently design a fixture of new appearance and then tool up to produce it commercially, instead of copying the fixture originated by another, these expenses are necessary. And I believe that the evidence will contrast such expenditures required by independent development of a design, such as the patented design, with the very small expenditures which were made by the defendant, and which I think the evidence will cause one to believe were avoided—the larger expenditures were avoided by the availability of the plaintiff's design, patented design, for imitation by the defendant. [98]

\* \* \*

Mr. Miketta: The defendant's end-piece, for example, is just a metal casting, that is, one casting. The plaintiff's device is pressed and stamped out of two pieces of material. One is a pressed thing, and this is a single piece of casting. Just because the plaintiff elected to make dies, to use pressure, and stamped it out of two pieces of metal, whereas the defendant cast his end in one piece, which would be of much less expense, doesn't mean a thing. [99]

\* \* \*

Now, why should we go into the question of costs, when the defendant doesn't even use that method of



(Testimony of Bertram A. Kaepfel.)

manufacture? I see no relevancy. We are just building up a record. The plaintiff is attempting to build up the case, I think, unnecessarily, and just cause us more damage.

\* \* \*

Mr. Foster: There is another ground for its materiality, however, your Honor, and that is that we believe that the appropriation of our design, indeed, we suggest its copying is an aggravation of the damage the plaintiff has suffered from its infringement. And frequently, many times, unfair competition to an extent less than actual copying has been held material, relevant and admissible evidence as an aggravation of damages. So it is offered on that ground, also. [100]

\* \* \*

The Court: Now, your design patent, your first patent, is a design, I take it, of the ends, the shape of the lamp housing, the shape and position of the louvers?

Mr. Foster: Yes.

The Court: All of which you claim is a part of your design?

Mr. Foster: Yes.

The Court: Now, the matter of the chassis would not have anything to do with it, would it?

Mr. Foster: True. [101]

\* \* \*

Q. (By Mr. Foster): I now direct your atten-

(Testimony of Bertram A. Kaepfel.)

tion to the '990 section, which shows the housing outline in the lower left-hand corner. That is Fig. 2. That was a part of the composite design of the patent?

A. Yes, sir. [102]

\* \* \*

The Court: Now, when you get all through going through Plaintiff's Exhibit 2, for identification, what is your purpose? To show you spent money?

Mr. Foster: Yes, sir.

The Court: And work in producing it?

Mr. Foster: Yes, sir, amounting to \$59,445.67, substantiated by the drawings made by this witness by his own hands on the dates they bear, and the invoices which are attached to this exhibit. We spent that amount of money to commercially produce it in the form now presented in the physical exhibit, that is, the patented design fixture. [103]

\* \* \*

Q. (By Mr. Foster): In Plaintiff's Exhibit 2, for identification, Mr. Kaepfel, there are tabbed with the letters A to F certain summaries and tabulations of expenditures; are those a summary and tabulation of expenses made by the plaintiff company in payments out for preparation of dies and tools outside its own plant for the commercial production of the patented design fixture, that is, the design of the patents in suit?

A. Yes, sir, those are all outside die costs.

Q. Are all those summaries of tabs A to F made by you or under your direction?

A. Yes, under my direction.

(Testimony of Bertram A. Kaepfel.)

Q. And from company records kept in the ordinary course of business, is that true?

A. Yes.

Q. Also listed in these tabs and lettered with various letters from A to Z and from AA to NN, there are a number [105] of drawings which are listed upon the table of contents in the front of the book; were all of those drawings made for the purpose of having such dies and tools produced for the commercial production of the fixture of the designs of the patents in suit?

A. Yes, sir, those are all detailed drawings for die work.

Q. And were they made by you?

A. They were all made by me.

Q. Were the drawings retained from the time they were made in the files of the plaintiff company engineering department?

A. Yes, sir. They are still on file.

Q. And as to any of them which bear dates, were the drawings completed on the dates which they bear, or within a day or two thereof?

A. Yes, sir.

Q. I notice among the lettered exhibits in Plaintiff's Exhibit 2 are some invoices; are those invoices which were paid by the plaintiff company for the work relating to the invoices and represented by the drawings in Plaintiff's Exhibit 2?

A. Yes, they are.

Q. And those invoices contained in Plaintiff's Exhibit 2, for identification, are typical of all of the invoices [106] paid by the plaintiff company

(Testimony of Bertram A. Kaepfel.)

for all of the work shown in the drawings of Plaintiff's Exhibit 1, for identification?

A. Yes, they are.

Q. And is the total sum shown by the summary on sheet A of Plaintiff's Exhibit 2 for identification, being \$59,445.67, the amount actually paid by the plaintiff after the perfection of the design of the patents in suit and for the commercial production of the fixtures embodying such design in dies and tooling up to produce the commercial fixtures bearing such designs? A. Yes.

Q. And in addition was any time spent within the plant of the plaintiff for that purpose?

A. Yes.

Q. And the additional time spent in the plant of the plaintiff is not shown in your summary?

A. No.

Mr. Foster: Plaintiff's Exhibit 2 with the various tabs, drawings and summaries, and bearing the letters A through Z and AA through NN, and the table of contents of that Plaintiff's Exhibit 2, for identification, are offered in evidence as Plaintiff's Exhibit 2, with the letters for each as shown in the table of contents. [107]

\* \* \*

The Court: Exhibit 2 is admitted into evidence.

Mr. Foster: May my offer of Plaintiff's Exhibit 1, your Honor, cover, also, the table of contents, and the reporter be asked to copy both of the tables of contents for the record?



(Testimony of Bertram A. Kaepfel.)

The Court: Yes, that will be done. However, I will say as far as your Exhibit 2 is concerned you can summarize that, as far as I am concerned, by saying that you spent money and time in developing your design.

I think when I have said that much I don't know that we get anything more from that document. Maybe you can convince me later that there is more in it than that.

(Thereupon, the exhibit marked Plaintiff's Exhibit 2, for identification, was received in evidence and the "Table of Contents" thereof is, in words and figures, as follows, to wit:)

A—Summary of Tool Costs.

B—Tabulation of 40-watt Chassis Die Costs.

C—Tabulation of 40-watt Enclosure Die Costs.

D—Tabulation of 40-watt Enclosure Die Costs  
(continued).

E—Tabulation of 85-watt Chassis Die Costs.

F—Tabulation of 85-watt Enclosure Die Costs.

G—Drawing Showing Spring Catch Arrangement for Removal of Enclosure from Chassis (Scale ten times full size:)

H—Drawing Showing Side Elevation (Scale ten times full size).

I—Drawing Showing Partial Section in Plan of Spring (Scale ten times full size).

J—Drawing Showing Chassis and Chassis Cover and Related Portion of Enclosure End (Scale ten times full size).

(Testimony of Bertram A. Kaepfel.)

K—Drawing Showing Relationship of Longitudinal Louver to Transverse Louver (Scale ten times full size).

L—Drawing Showing Relationship Between Louver Panel Formation and Transverse Louver (Scale ten times full size).

M—Drawing of Side Panel Stretchout #S-18468 (Scale full size).

N—Drawing of End Insert #SW-20248 (Scale full size).

O—Atlas Invoice No. 25964.

P—Drawing of Lateral Louver #PKW-20407 (Scale full size).

Q—Atlas Invoice No. 25962.

R—Atlas Invoice No. 25965.

S—Drawing of End Cover #PKW-18598 (Scale full size).

T—Atlas Invoice No. 25963.

U—Drawing of Wiring Cover, End Notch and Perforation #PK-18569 (Full size).

V—Atlas Invoice No. 26342. [109]

W—Drawing of Longitudinal Louver Stretchout #PK-18467 (Full size).

X—Atlas Invoice No. 26341.

Y—Drawing of Socket Box #PK-18559 (Full size).

Z—Atlas Invoice No. 25957.

AA—Atlas Invoice No. 25958.

BB—Atlas Invoice No. 25959.

CC—Atlas Invoice No. 26338.

(Testimony of Bertram A. Kaepfel.)

DD—Drawing of Side Panel Stretchout #PK-20166 (Full size).

EE—Atlas Invoice No. 26340.

FF—Drawing of End Piece #PK-18283. (Full size).

GG—Omar Job No. 11201.

HH—Atlas Invoice No. 26333.

II—Atlas Invoice No. 26334.

JJ—Drawing of Long and Short Mounting Channel #PKW-20163 (Full size).

KK—Atlas Invoice No. 25960.

LL—Atlas Invoice No. 26339.

MM—Drawing of Channel Stretchout.

NN—Drawing of Channel Stretchout #PK-18475. [110]

\* \* \*

Q. (By Mr. Foster): Mr. Kaepfel, have you made any comparisons of the dimension and design features of the Ruby Paramount accused design and the Day-Brite patented design? A. Yes, I have.

Q. Did you make any drawing comparing the appearance and dimensions of the end plates of those two fixtures?

A. Yes, sir, I have the composite drawing.

Q. I direct your attention to the drawing marked I of Plaintiff's Exhibit 11, for identification, and ask you if that is the drawing to which you refer.

A. Yes, sir, I made that drawing.

Q. Would you explain what is represented by this drawing tab I of Plaintiff's Exhibit 11, for identification, and how you made it?

(Testimony of Bertram A. Kaepfel.)

A. It was made by taking each of the fixtures in turn and tracing around the contours of the end.

Q. Upon a thin sheet of paper that you have as that exhibit, is that correct? A. Yes.

Q. Are the legends that appear upon here correct, that is, the number of the transverse louvers of both equal 13? [111] A. Yes, sir.

Q. And the overall length of both equals 48-7/16 inches? A. Yes, sir.

Q. Did you measure these angles and put the number of degrees of the angles shown on this drawing? A. Yes, sir.

Q. And the overall height of the ends of the two fixtures? A. Yes, sir.

Q. And are all of the angles and all of the dimensions shown numerically upon this drawing tab I of Plaintiff's Exhibit 11, for identification, correct within the allowance of working tolerances?

A. Yes, sir, they are.

Mr. Foster: The drawing tab I of Plaintiff's Exhibit 11, for identification, is offered into evidence as Plaintiff's Exhibit 11-I, your Honor.

The Court: It will be received in evidence, tab I of Exhibit 11.

\* \* \*

Mr. Foster: I might state, your Honor, that as depicted upon Plaintiff's Exhibit 11-I showing only the end plates, plus the number of louvers, plus the overall length of the [112] fixture, there are seven



(Testimony of Bertram A. Kaepfel.)

identities shown by this exhibit to exist between the plaintiff's commercial patented design fixture and the defendant's accused structure. Subsequent testimony will show that it is very improbable this could have been coincidental.

Q. (By Mr. Foster): Could the dimensions shown upon that drawing to which you last referred, and the angles, have been of any other values without detracting from the utility of those fixtures?

A. Yes.

\* \* \*

Q. (By Mr. Foster): I note that upon Plaintiff's Exhibit 11-I there is a  $7\frac{1}{2}$  degree angle in the upper and lower edges of the end plates. Why was that particular angle chosen?

Mr. Miketta: That is objected to, your Honor, as calling for a conclusion.

The Court: The way the question is asked, it is very broad. Do you mean why it was chosen by this witness for use in the plaintiff's device? [113]

Mr. Foster: Yes.

Q. Why was it chosen by you, Mr. Kaepfel, for the plaintiff's end caps on their fixture?

The Court: Do you have an objection now?

Mr. Miketta: I guess not. I misunderstood the question.

The Witness: It was chosen because it is a pleasing angle, it blended in with all the other angles and lengths of sides and bottom.

Q. (By Mr. Foster): Were the  $7\frac{1}{2}$  degree

(Testimony of Bertram A. Kaepfel.)

angles of the plaintiff's patented design end plate chosen because of any utility reasons?

A. No, sir.

Q. So far as you know, and so far as utility is concerned, the  $7\frac{1}{2}$  degree angles could have been no angles at all but horizontal edges or angles of different value than  $7\frac{1}{2}$  degrees? A. Yes.

Q. Is the same thing true of the  $22\frac{1}{2}$  degree angle shown in the same exhibit?

A. Yes, sir, that is the angle of the side.

The Court: Do I understand from Plaintiff's Exhibit 11-I that that 22 degree angle was the same on the side of both the Day-Brite patented structure and the Ruby accused structure? [114]

The Witness: Yes, your Honor.

The Court: On the right-hand side of the chart the straight lines and the dotted lines would appear to have somewhat different angles.

Q. (By Mr. Foster): Would you explain that, please, Mr. Kaepfel?

A. Yes. I would say that is due to the fact that on the Day-Brite fixture ours is a stamping, it is made to much closer tolerances than a casting, which is made by less experienced and less skilled men, and therefore the angles of the two sides could be slightly different.

Q. Is there anything done to the castings of the Ruby accused design end plate after they are taken out of the casting or mold? A. Yes.

Q. That would affect this angle?

A. Yes, all castings are either ground or polished

(Testimony of Bertram A. Kaepfel.)

as a final finishing process, and depending upon the coarseness of the casting they would need either more or less grinding.

Q. Would the variations of the  $22\frac{1}{2}$  degree angle sides of the Ruby accused design castings from the full line shown in this exhibit Plaintiff's 11-I, be variations within working tolerances allowing for the polishing and the casting operation?

A. Yes, sir. [115]

Q. I notice that a vertical wall is chosen at each side of the central upwardly projecting top portion of these end plates on Plaintiff's Exhibit 11-I. Why were those walls vertical instead of an angle from the vertical? Any utility reason for your selecting that vertical wall?

A. Could I have that question again, please? I don't quite understand you.

Q. Yes. I note in this Plaintiff's Exhibit 11-I in the central upper part of the end plates of the Ruby accused design and the Day-Brite patented design there is a vertical wall at the top of that upper projecting portion instead of a wall which might be at an angle with the vertical. Did you select that vertical wall instead of an angle wall for utility reasons? Is my question clear to you?

A. Actually we have a large radius, and then we go into the vertical wall.

Q. My question is could these vertical walls at the top of the end plates have been made at an angle with the vertical?

(Testimony of Bertram A. Kaepfel.)

A. Yes, they could have been anything, surely

Q. And were those vertical walls chosen, then, for appearance reasons? A. Yes.

Q. In the Day-Brite commercial fixture do you find on the sides of the fixture two rectangular panels about midway [116] of the sides?

A. Yes, sir.

Q. And do you find any panels of like nature upon the Ruby accused fixture?

A. Yes, sir, there are similar panels.

Q. As I understand your testimony, then, all of the things indicated upon your drawing Plaintiff's Exhibit 11-I as identical in end plates, number of transverse louvers, and overall length were selected by you in the Day-Brite fixture for their appearance value and not for utility reasons, is that true? A. That is true.

Q. And all of those things thus indicated, the dimensions, angles, number of louvers, and length, could have been varied to any one of a great number of alternative values without detracting from the utility of the fixture, is that true?

A. Yes, sir, it is true.

Q. And each individually and all of them in the aggregate were selected by you entirely for their appealing appearance? A. Yes, sir.

Q. And that would include the width and height of the end plate, as well as all of the angles shown on this Plaintiff's Exhibit 11-I, is that correct?

A. Yes, true. [117]



(Testimony of Bertram A. Kaepfel.)

Mr. Foster: That is all of the direct examination of this witness. [118]

\* \* \*

### Cross-Examination

By Mr. Miketta:

The Court: Proceed.

Q. Mr. Kaepfel, do you know of the Electric Testing Laboratories?

A. Yes, sir, I have heard of them.

Q. Do you know what they do?

A. To the best of my knowledge, they test electrical equipment.

Q. Have you ever seen any reports published by the E.T.L.?

A. Yes, sir; I have seen them.

Q. And those reports on fixtures manufactured by the plaintiff concern are obtained by the plaintiff, are they not?

A. May I have that question again?

Q. Does the plaintiff obtain reports on its fixtures from E.T.L.?

A. Yes, sir.

Q. And those charts or graphs are published by the plaintiff? [125]

A. Yes, sir.

Q. Now, those graphs and charts show the distribution of light from a fixture; is that right?

\* \* \*

The Witness: It is correct.

Q. (By Mr. Miketta): In which directions or along what axis is that distribution shown?

(Testimony of Bertram A. Kaepfel.)

A. I don't know that I am very well qualified to speak on that.

Q. You don't know anything about the distribution of light from an electric fixture?

A. I know merely that the fixtures are tested in three different planes, and that is as far as my knowledge goes.

Q. And which are the planes?

A. The planes would be vertical longitudinal, vertical lateral, and a vertical plane bisecting those two.

Q. In other words, a plane taken lengthwise, a vertical plane taken lengthwise of the fixture? [126]

A. Yes, sir.

Q. Another plane, vertical plane, transverse to the fixture?      A. Yes, sir.

Q. And then another plane at an angle to those?

A. Bisecting the two, at a 45-degree angle.

Q. At a 45-degree angle?      A. Yes, sir.

Q. Very well. Do you know whether the distribution of light is measured both above the axis of the lighting fixture, longitudinal axis of the lighting fixture, as well as below that axis or plane?

A. Yes, it is.

Q. It is. Now, you have been with Day-Brite since 1935; is that correct?

A. It is correct.

Q. What are your duties and activities?

A. My duties concern themselves primarily with the procurement of proper tooling and machinery for production of lighting fixtures. I also do a

(Testimony of Bertram A. Kaepfel.)

good deal of design work, that is, assist in the designing of lighting fixtures.

Q. Now, those are your present duties; is that correct?      A. Yes, sir.

Q. What were they in 1935? [127]

A. In 1935, when I joined the company, I was hired for the purpose of making drawings of lighting fixtures.

Q. What did you do, or, how did your work enlarge after that?

A. I beg pardon? I didn't hear that.

Q. Did you change your activities as you stayed with the company?

A. Yes, those activities changed right along. I gradually became responsible for more and more work.

Q. Now, being in charge of production, you may say, of tools and dies, when did you first start doing work which pertained to the manufacture or the arrangement of dies used in fabricating fixtures?

A. It is difficult to pin that down to an exact date——

Q. To your best recollection.

A. ——because I started in by helping someone else do that work. To the best of my recollection, it would be about 1939 or '40; around in there.

Q. Are you an engineer?

A. I am a member of the American Society of Tool Engineers. I am not a registered engineer.

Q. Now, in the design of fixtures, you take into

(Testimony of Bertram A. Kaepfel.)

consideration the production difficulties that might arise in making such a fixture, do you not?

A. Very definitely, yes, sir. [128]

Q. So that you are familiar with fabrication of parts and their assembly? A. Yes, sir.

Q. Are you familiar with progressive dies?

A. Yes, sir.

Q. And lancing dies? A. Yes, sir.

The Court: Lancing?

Mr. Miketta: Lancing, yes, your Honor.

Q. (By Mr. Miketta): That is a perforating die, is it not, Mr. Kaepfel?

A. Yes, sir. It partially perforates and partially forms.

Q. In your engineering experience and production in dies and tooling, you have taken into consideration the strength of the materials employed; is that correct? A. Yes, sir.

Q. And the necessity of reinforcing it, if the occasion so warrants; is that right?

A. That is correct.

Q. Have you ever done any sales work?

A. No, sir.

Q. Now, you are familiar with the various fixtures made by Day-Brite, are you not?

A. Very familiar. [129]

Q. How many different fixtures do they make?

A. I don't think that I could state that without guessing.

Q. Well, what is your best guess? I am not talking about the number that they manufacture



(Testimony of Bertram A. Kaepfel.)

per year, Mr. Kaepfel. I am not interested in that, but just in the different types that they make. Of course, they make a two-tube unit, do they not?

A. We make a one-tube, two-tube, three-tube, four-tube; anything the customer will require.

Q. That is right. Now, let's just talk about the two-tube and the four-tube fixtures. Approximately how many different types of fixtures does Day-Brite make in just these two categories?

\* \* \*

The Court: What is the least number you certainly make in, we will take the two-tube class? They make more, but you are certain they make how many styles in the two-tube [130] class?

The Witness: It can be resolved by saying we make no less than ten.

Q. (By Mr. Miketta): Not less than ten different styles; is that right?

The Court: In the two-tube class.

The Witness: Yes. [131]

\* \* \*

The Court: What is the least number that you are certain of in the four-tube class?

The Witness: I would have to have some time to stop and think, see exactly what it is that we make.

The Court: They make one, don't they, in the four-tube class, one standard type, to start with?

The Witness: Let us say that it is six as a

(Testimony of Bertram A. Kaepfel.)

minimum of two-lamp fixtures that we make of the standard type.

The Court: Two-tube?

The Witness: Of the two-tube, yes.

Q. (By Mr. Miketta): How about the four-tube?

A. Four could be used as a minimum number of four-lamp [132] standard fixtures.

\* \* \*

Q. Very well. Do those fixtures vary in length?

A. If I understand the question correctly, they do not vary in length individually. The different classifications of fixtures may vary somewhat.

Q. In other words, if you are making fixtures to accommodate the so-called 48-inch fluorescent tube, then all of the fixtures that are supposed to receive 48-inch tubes are of substantially the same length, is that correct?

A. They would be subject to differences as great as  $\frac{7}{8}$  of an inch.

Q. Very well. So you would call  $\frac{7}{8}$  of an inch, you might say, your manufacturing tolerance, is that correct?

A. No; that is a design tolerance.

Q. Do you also make fixtures to accommodate shorter tubes?

A. Yes, sir, we make fixtures for the 18-, 24-, 36-inch tubes, also.

Q. So that 36-inch tubes will take a fixture that is built to accommodate 36-inch tubes, and if you want a fixture to take 48-inch tubes, you build a

(Testimony of Bertram A. Kaepfel.)

fixture to accommodate that, is that correct?

A. If by "accommodate" you mean that the fixtures [133] themselves are the exact length of the tubes, that is not the answer.

Q. That was not the premise.

The Court: Read the question.

Q. (By Mr. Miketta): I understand that there are end pieces which are outside the end of the 48-inch tubes, so that your overall fixture is probably a little longer than 48-inches.

A. That's right.

Q. But in a fixture which accommodates a 36-inch tube, the end plates are just slightly more than 36 inches apart, is that correct?

\* \* \*

The Witness: The answer to that would be that we do have some fixtures which would run a matter of several inches over the lamp length.

Q. (By Mr. Miketta): But a fixture that is built to accommodate a 36-inch tube would not actually receive and operatively hold a 48-inch tube, is that correct? [134]

A. That is correct, yes, sir.

Q. I would like to have you refer to Plaintiff's Exhibit 1. I understand that you made these sketches personally, is that right?

A. That is correct.

Q. Is that correct?           A. Yes, sir.

Q. At the time that you were working on these sketches, were there any other draftsmen being employed by Day-Brite?

(Testimony of Bertram A. Kaepfel.)

A. Yes, there were certainly three or four other draftsmen.

Q. Were you in charge of that department, Mr. Kaepfel?      A. No, sir, not at that time.

Q. Who was in charge of that department?

A. Do you want the man's name?

Q. I asked the question.

A. Mr. John Gornet, G-o-r-n-e-t.

Q. Were these made under his supervision?

A. Yes, they were.

Q. Who directed you to start this work which you did in designing a fixture?

A. I started it under my own authority.

Q. In other words, this was an independent enterprise, [135] you weren't told to do this by anyone?      A. Yes, sir.

Q. Who authorized the making of the various mockups to which you referred?

A. I authorized those, also.

A. I didn't hear you.

A. I authorized those, also.

Q. No one else had anything to do with them?

A. Not directly.

Q. This man who was in charge of the engineering department, didn't he have anything to say about that?

A. He has many other duties, and it isn't always incumbent upon him to be immediately responsible for work of this type.

Q. But the cost of making the mock-ups was such an insignificant sum that you authorized it,



(Testimony of Bertram A. Kaepfel.)

you just went ahead and had them made, is that correct?

A. If \$100 is an insignificant sum, that is correct.

Q. But you didn't need any special authorization or appropriation, as a matter of fact no actual order was given by anyone in authority to have this designing work done or to have the mock-ups made, isn't that correct?

A. It is correct that I had sufficient authority to initiate that order. [136]

Q. Why did you start designing a two-tube fixture and not a four-tube fixture?

A. Because it seemed to me that the demand for the two-tube fixture would be much greater than the demand for the four-tube fixture.

Q. You had no sales experience you told me; how did you know that?

A. I have had much opportunity to talk with salesmen and representatives of the company when they come to the home plant for a visit.

Q. But personally you did not do any sales work, am I correct?      A. That is correct.

Q. What length fixture did you start designing when you started to do the work which is shown in Exhibit 1?

A. We started designing a fixture for a 48-inch tubular lamp.

Q. So that the length of the fixture was established as soon, that is, within narrow limits, as soon as you decided to use a 48-inch tube, is that correct?

(Testimony of Bertram A. Kaepfel.)

A. The minimum length was established at that time.

Q. Exhibit 1-A is a sketch of a housing for the ballast and the reactors, and apparently to hold the sockets for the end of the tube, isn't that correct?

A. That is correct. [137]

Q. That sketch indicates a two-piece housing, does it not? A. It does, yes, sir.

Q. That is, it has an upper part and a lower part? A. Correct.

Q. Do you still use a two-piece housing in the fixture which is before the court here?

A. Yes, sir, we still do.

\* \* \*

Q. The two-piece housing, how is that held together?

A. The wiring cover is snapped onto the back channel.

Q. Is it not a fact, Mr. Kaepfel, that the [138] two-piece housing is shown and described in Plaintiff's Exhibit 5, which is Patent No. 2,411,952? You are familiar with that patent, aren't you? That is the one that was issued in 1946 on an application filed in 1944.

\* \* \*

The Witness: The answer is that this patent No. 2,411,952 does show the snapped-on cover.

Q. (By Mr. Miketta): Are you familiar with the marking that appears on the fixtures which embody the patented design? [139]

(Testimony of Bertram A. Kaepfel.)

\* \* \*

Q. This patent number to which you refer, 2,411,952, does it appear on that fixture, Plaintiff's Exhibit 13?

A. Do you mean the patent number itself, is it engraved on the fixture?

The Court: Printed, engraved, stamped——

The Witness: No, sir, it is not.

Q. (By Mr. Miketta): Are there any patent numbers that are marked or engraved on that fixture?

A. There are none that I know of.

Q. Now, the can or housing which you show here on Exhibit 1-A could also be used in any other two-tube fixture, is that correct?

A. "Any other" would be a rather broad statement. It would depend upon the enclosure to be used with this chassis or can, as you refer to it.

Q. Well, without quibbling, could you admit that it could be used on other fixtures?

A. It can be used on other fixtures, yes.

Q. And are you actually using the split-housed can or housing on fixtures other than the fixture identified here as Exhibit 13?

A. Yes, sir, we are.

Q. Why did you perforate the end plate on the fixture which is shown in the two patents in suit here, Plaintiff's Exhibits 3 and 4, and which is supposed to be embodied in [140] Plaintiff's Exhibit 13?

A. If I understand the question, you are refer-

(Testimony of Bertram A. Kaepfel.)

ring to the ornamentation in the end of the viz-aid fixture. The perforations were put there for purely ornamental or decorative purposes.

Q. By such perforations and ornamentation you are referring to the light-colored portions which are visible in the end plate of Exhibit 13?

A. Yes, sir, I am.

Q. How would you describe those perforations, that is, their form? Zigzag form?

A. Yes, zigzag or modified S-shape.

\* \* \*

Q. Is it not true, Mr. Kaepfel, that those are perforations in the end plate, and you have a louver in back of it that is a separate member?

A. Yes, sir, there is a backing-up plate.

Q. So that the end plate itself is perforated?

A. Yes, sir.

Q. In the course of your 15 years of work with the Day-Brite Company, the plaintiff here, and prior to the work that you started and which is referred to in Exhibit 1, were [141] you familiar with other fluorescent fixtures that were being manufactured by other manufacturers?

A. I was familiar with them to the extent that I would see illustrations in catalogs which, naturally, we were interested in.

Q. Well, you made a collection of all the catalogs relating to fluorescent fixtures that you could find, did you not?      A. Yes, sir.

Q. That is customary in all manufacturing plants?      A. That is customary.



(Testimony of Bertram A. Kaepfel.)

Q. You were familiar with the Wakefield line, the Miller line, were you not?

A. The word "familiar" is a rather broad one. I knew of them and knew of some of the individual fixtures.

Q. And you had seen illustrations of those fixtures?      A. Yes, sir.

Q. And is it not a fact that in most of the catalogs published by manufacturers of lighting fixtures they give you a little diagram giving the height and the width of the end plate, you may say, or cross-section, so that an architect knows how it will fit in or how far it will extend from the ceiling?

A. Yes, sir, that is so.

Q. So that prior to 1943 you had seen fixtures manufactured [142] by others which had longitudinally extending, outwardly inclined side panels, had you not?      A. There may have been. [143]

\* \* \*

Q. (By Mr. Miketta): I show you Plaintiff's Exhibit 9 which is in evidence, and particularly, a sheet bearing the letter "H," which shows a Challenger fixture. Does that fixture have downwardly or upwardly and outwardly inclined side panels?

A. Yes, sir, it does. [144]

\* \* \*

Q. (By Mr. Miketta): Were those panels translucent?

\* \* \*

(Testimony of Bertram A. Kaepfel.)

The Witness: They were.

Q. (By Mr. Miketta): Do you know why in a fluorescent lighting fixture those side panels are made translucent?

A. They would be made translucent for the improved appearance of the fixture.

Q. Is that the only reason?

A. There would also be more emitted light.

Q. And the light is emitted to the side, is it not?

A. Yes, sir, it is.

Q. And downwardly?

A. Outwardly or downwardly, yes, sir.

Q. Now, the bottom of this fixture which is shown in Exhibit 9-H was open. It did not have any solid sheet; is that correct? A. Yes, sir.

Q. And it had both longitudinal and transverse louvers in the bottom of that fixture, did it not?

A. As shown on the drawing, it does have those.

Q. Do you know what the purpose is of both longitudinal and transverse louvers in the bottom of a fluorescent fixture? [145]

A. Yes, sir, I do.

Q. What is the purpose?

A. To shield the lamp from the eye of the viewer.

Q. In other words, you want to prevent an observer from looking directly in the tube; is that correct? A. That is one purpose, yes, sir.

Q. What is the other purpose?

A. The other purpose would be for the appearance of the enclosure and the whole.

(Testimony of Bertram A. Kaepfel.)

Q. Is it true from an examination of this exhibit and whatever you know about this fixture that the bottom of that fixture is not flat, but is inclined?

A. The picture shows that the sides are inclined, —the bottom is inclined, yes, sir.

Q. Towards the center line? A. Yes, sir.

Q. And the spacing between the transverse louvers in a fixture depends upon the distance of that louver from the fluorescent tube, so as to get the proper cut-off angle at which an observer would not see the tube; is that correct?

\* \* \*

Q. (By Mr. Miketta): And perhaps you may want to add [146] another factor; that the height of the louver also influences the spacing that you would have between the louvers, to give you a cut-off angle?

A. That is right. That is correct.

Q. Now, by referring to the preceding exhibit in Plaintiff's Exhibit 9, the one preceding H, —

The Court: G?

Mr. Miketta: Yes, your Honor.

Q. (By Mr. Miketta): —and particularly to page 14, I call your attention to the lighting fixture which is shown in the lower right-hand corner of page 14.

\* \* \*

Q. (By Mr. Miketta): That also has translucent sides; is that correct? A. Yes, sir. [147]

(Testimony of Bertram A. Kaeppel.)

Q. And they are inclined upwardly and outwardly; is that correct? A. Yes.

Q. And it has a louvered bottom provided with both transverse and longitudinal louvers; is that correct? A. Yes, sir.

Q. And the end of that fixture is provided with a central boss or upright portion which is higher than the edge portions of that end, the upper edge portions of that end; is that correct?

Mr. Foster: I object to that question and to this line of questioning on the ground that these documents speak for themselves. He is asking him whether a device shows so-and-so, or it does so-and-so. The best evidence is the illustration itself.

Mr. Miketta: I am laying a foundation.

The Court: The witness has testified that these were some of the designs that he saw before he worked on his.

Mr. Foster: That hasn't been testified to, your Honor.

The Witness: No, sir.

The Court: What is that?

The Witness: No, your Honor. [148]

\* \* \*

The Witness: The drawing shows such upward projection.

Q. (By Mr. Miketta): Now, fixtures of this type can be suspended from a ceiling in several ways, can they not?

A. That is a rather broad statement.



(Testimony of Bertram A. Kaepfel.)

\* \* \*

Q. Can your own fixture be suspended from the ceiling, either in close contact with the ceiling or from standards or pedestals?

A. Yes, sir, it can.

Q. Have you seen other fluorescent fixtures also suspended from ceilings in those two ways?

A. Subsequent to our fixture, yes, sir.

Q. But you had never seen it previously to that time, any other fluorescent fixture hung in any other way, or in that way?

A. I may have without being able to state positively "Yes" or "No" at this time.

Q. You did see pictures of various fixtures, did you [149] not?

The Court: You mean before he made his?

Q. (By Mr. Miketta): Before you started designing your own?

A. Undoubtedly I have, yes, sir. [150]

\* \* \*

Q. (By Mr. Miketta): Have you seen fixtures hung in the manner of Exhibit 14 in the court room here previously to today or yesterday?

A. Yes, sir, previously to today or yesterday.

\* \* \*

Q. (By Mr. Miketta): Now, when a fixture's hung in the manner before you here, is there any light which is thrown up against the ceiling?

A. Yes, sir. A certain proportion of the light would be thrown upward against the ceiling.

(Testimony of Bertram A. Kaepfel.)

Q. If you didn't have that step-down or the fact that you have a central upstanding portion in the upper edge of the end, you would not have any light thrown up against the ceiling; is that correct?

A. That is correct.

Q. I understand that the Day-Brite fixture, Exhibit 13, can be easily relamped; is that true?

A. That is true.

Q. Could you demonstrate that, please?

The Court: You may step down. [152]

\* \* \*

Q. (By Mr. Miketta): Will you demonstrate the manner in which it can be readily relamped?

(The witness does as requested.)

Q. (By Mr. Miketta): Now, if it was hung from the ceiling, how would you do that?

The Court: Let the record show the witness has taken out one of the fluorescent tubes.

The Witness: It can be done in the very same manner. There is sufficient room between the upper edge of the side member and the ceiling to permit this type of relamping at any time.

Q. (By Mr. Miketta): Is it not a fact that the entire bottom portion of this frame comes off?

A. Yes, it is a fact.

Q. And isn't that the way it is relamped—

A. Not necessarily.

Q. —when the thing is hung on the ceiling?

A. Not necessarily.

(Testimony of Bertram A. Kaepfel.)

Q. Will you demonstrate how it comes apart?

(The witness does as requested.)

The Witness: I am at a physical disadvantage here because of a manual disability, and, of course, the means of [153] mounting here. With the fixture properly in place, it is a matter of seconds.

Mr. Miketta: Let the record show that the witness has lowered the frame of the fixture——

The Court: Exhibit 13.

Mr. Miketta: ——Exhibit 13 from the upper portion, which constitutes the chassis and the fluorescent tubes and includes an end cover.

The Court: That now the bottom portion hangs by a chain from what you have called the can.

Mr. Miketta: The can or chassis. [154]

\* \* \*

Q. (By Mr. Miketta): Mr. Kaepfel, you are familiar with the literature published by the plaintiff in this case, are you not?

A. Yes, sir, I am.

Q. I show you Bulletin 10——

The Court: Has it been marked for identification?

Mr. Miketta: May I have it marked for identification, please?

The Clerk: Defendant's Exhibit A for identification.

\* \* \*

Q. I show you Defendant's Exhibit A for iden-

(Testimony of Bertram A. Kaepfel.)

tification, a Bulletin No. 10-B-1, allegedly published August, 1946; you have seen this previously?

A. Yes, sir, I have.

Q. Do you identify it as a publication of the plaintiff? A. Yes, sir, I do.

The Court: What date?

Mr. Miketta: August, 1946, your Honor.

Q. I call your attention to page 8 of that bulletin, and particularly the illustration appearing in the upper section. [155] Does that pictorially describe and show the manner in which the frame of the fixture can be removed from the chassis or suspended from the chassis in the manner which you have just demonstrated to the court?

A. Yes, sir, it does.

Q. I call your attention to page 6 of that bulletin, particularly the lower portion headed "All fixtures use this same basic chassis"; does that show the chassis which is employed in the Exhibit 13 which you have demounted?

A. Yes, sir, it does.

Q. And it is my understanding that the construction of the chassis illustrated on page 6 is that which is described in Plaintiff's Patent Exhibit 5, is that correct? A. Yes, sir, it is.

Mr. Miketta: I ask that the exhibit identified by the witness be introduced in evidence as Defendant's Exhibit A, your Honor.

Mr. Foster: It is a duplication, Mr. Miketta, of Plaintiff's Exhibit 6-K, the same catalog.



(Testimony of Bertram A. Kaepfel.)

Mr. Miketta: Well, I would like to have this separately, please.

The Court: It may be received as Defendant's A in evidence. [156]

\* \* \*

Q. (By Mr. Miketta): Now, Mr. Kaepfel, again referring to Exhibit 1, which of those drawings is a drawing of the design in the patent in suit?

A. It would be represented by the letter E and the letter D.

Q. Both of them represent the design of the patent in suit?      A. Yes, sir.

Q. Well, I would like to call your attention to Plaintiff's Exhibit 3 and ask you to point out wherein in Exhibit D or section D of Plaintiff's Exhibit 1 do you find the round bead at the bottom end of the V-shaped louver which is illustrated in figures 1 and 2 of patent 138,990.

A. You do not find that on these drawings, because——

Q. By "these drawings" you refer to Exhibit 1-D?      A. Yes, sir, or 1-E.

Q. Therefore the drawings 1-D and 1-E do not show the rounded bead which is a characteristic of the design in design patent 138,990, Plaintiff's Exhibit 3, is that correct? [157]

\* \* \*

The Witness: The answer to that would be that the bead as shown in the patent drawing was at

(Testimony of Bertram A. Kaepfel.)

one time and for about a period of one year on these drawings.

Q. (By Mr. Miketta): Well, then, have these drawings, Exhibit 1-D and -E been altered.

A. They have been altered as indicated by change letters A and B on Exhibit 1-D, and as indicated by revision B on Exhibit 1-E.

Q. There are two letters, both A and B adjacent the central figure of Exhibit 1-D. What do they mean?

A. Those small figures indicate that a revision took place and are identified by the revision letter as such.

Q. Were those revisions made prior or after the date appearing on Exhibit 1-D?

A. They would be made after that date.

Q. I thought you testified, Mr. Kaepfel, that these drawings were made on the date shown on these drawings.

A. The original drawing was made on the date shown on Exhibits D and E, respectively, but they are subject to change as we improve the fixture.

\* \* \*

Q. (By Mr. Miketta): Let me get this straight. On 6-22-44, which appears on Exhibit 1-D as it was originally made on 6-22-44, was the drawing in the same condition that we now see it, or was there a rounded bead at the end of that V-shaped louver?

A. On 6-22-44 there was a circular bead extending the full length of the central V-shaped louver.

(Testimony of Bertram A. Kaepfel.)

Q. And at some subsequent date that was erased and that bead was taken out, is that correct?

A. That is correct.

Q. On what date was that taken out?

A. It is not discernible on these photostatic copies. It may be discernible on the court's copy.

(Exhibit handed to the witness.)

The Witness: Revision B on the drawing dated 6-22-44 indicates a change 9-16-46.

Q. (By Mr. Miketta): And that is the change from the rounded bead to a straight-sided V, is that correct?

A. It is either that one or revision A dated 6-28-45. The exact sequence of those changes escapes me at the moment.

Q. Now, I call your attention to the sketch appearing on the right-hand side of Exhibit 1-D and ask if that does not show that the side rail at the top of the frame and at the bottom of the frame was joined together by three spaced [159] bars, each of them having an embossed bead.

A. Yes, it shows that on the drawing.

Q. There was no change made in that, was there, since 6-22-44?

A. Since that date there has been no change.

Q. So that that is a part of the design, is that correct?

A. Yes, sir, that is correct.

Q. I call your attention to figure 1 of design patent 138,990, that is Plaintiff's Exhibit 3, and ask if you can find there three parallel bars each with an emboss thereon.

(Testimony of Bertram A. Kaepfel.)

A. The design patent drawing does not show the emboss. It shows the three parallel bars.

Q. But it does not show the emboss?

A. No, it does not.

Q. I call your attention to Plaintiff's Exhibit 13, which is the plaintiff's fixture, and ask if that fixture at its side has upper and lower rails connected with three parallel bars each with an embossing on it?

A. Yes, sir, the exhibit shows that. [160]

\* \* \*

Mr. Miketta: Very well. I will change my question if Mr. Foster so desires and ask a leading question.

Q. Does the cover plate illustrated in figure 1 of Exhibit 3 include a round protuberance?

A. Yes, sir, it does include a protuberance.

Q. And that is within a recessed area of that cover plate, is that correct?

A. Yes, sir, it is.

Q. I call your attention to Plaintiff's Exhibit 13 and the cover plate on the end of the chassis and ask if you find in Plaintiff's Exhibit 13 a round protruding boss within the recessed area of that end plate.

A. No, sir, there is not.

Q. Now, I ask you to look at Plaintiff's Exhibit 15, which is the defendant's four-tube fixture, and ask if you find in that fixture a separate cover plate for the chassis.

A. No, sir, there is not.

Q. Do you find the circular boss which appears



(Testimony of Bertram A. Kaepfel.)

in figure 1 of Exhibit 3 in the end plate or the end of Plaintiff's Exhibit 15?

A. No, sir, there is not.

Q. Have you examined Exhibit 15 previously?

A. No, sir, I have not.

Q. Have you had a chance to work with it or take it apart?

A. No, sir, I have not.

Q. You did make a sketch of the end, did you not?

A. Not of that exhibit at all.

Q. Was it of the two-tube fixture?

A. It was of the two-tube fixture. [162]

\* \* \*

Q. Can you see that end on Exhibit 14?

A. Yes, sir.

The Court: Referring now to the end to which the electric wire is attached.

Mr. Miketta: Very well.

Q. Does that have a separate end cap for the chassis as is true in Plaintiff's Exhibit 13?

A. No, sir, it does not have.

Q. Does it have the circular boss within a recess to which you have previously referred?

A. The end that I can see here has no separate boss. [163]

Q. Very well. Now, let's turn it around. Now, I call your attention to the other or opposite end of the fixture, Exhibit 14, the one through which the light cord is not attached, and ask if that has a separate cover-plate for the chassis.

A. No, sir, it does not have.

Q. Does it have a protruding boss within a recess?

(Testimony of Bertram A. Kaepfel.)

A. There is a protruding boss, but not within a recess.

Q. To what extent does that protrude, Mr. Kaepfel?

A. That would be difficult to say from here.

Q. Well, during the noon recess——

The Court: Let's get a stipulation on that right now?

Mr. Foster: How long do you say it protrudes?

Mr. Miketta: I would say about 1/16 of an inch.

Mr. Foster: I will so stipulate. I think that is right.

The Court: To the court, who is sitting approximately 15 feet or 16 feet from it, that particular boss appears to be about the size—a little bigger than a nickel and smaller than a quarter in diameter.

Mr. Miketta: That is correct.

Q. (By Mr. Miketta): Mr. Kaepfel, is it not a fact that that little circular protrusion to which you have referred is termed a knock-out?

A. That boss is a knock-out plug. [164]

Q. That is for the purpose of making connections from one fixture to the other when those fixtures are in abutting aligned relation; is that correct? A. That is correct.

Q. On the fixture, Plaintiff's Exhibit 15, that knock-out has been knocked out of both ends of the fixture; is that correct?

A. Yes, sir; there is no plug in those holes.

(Testimony of Bertram A. Kaepfel.)

Q. (By Mr. Miketta): Now, then, Mr. Kaepfel, you stated [165] that the bead in the bottom of the V-shaped louver was used to attach the louver to the end; is that correct?

A. The bead was originally used for that purpose, yes, sir.

The Court: To make a hole, and that is where the screw went in?

The Witness: Yes. The bead was used as a hole for a thread-cutting screw.

Q. (By Mr. Miketta): Therefore, you did not have to use a bracket or drill a separate hole in order to make the connection; is that correct?

A. That is correct.

Q. While we still have the exhibits here, though, I want to call your attention to one other fact. Is it true, Mr. Kaepfel, that the V-shaped longitudinal louver of the plaintiff's device, Exhibit 13, is made of a specular or mirror-like material?

A. That is correct; it is.

Q. In other words, it gives a mirror-like reflecting surface on the outside? A. It does.

Q. Now, the defendant's devices, such as Exhibits 15 and 14, do not use a mirror-like surface on the longitudinal louver, do they?

A. They do not. [166]

Q. Thank you. I call your attention to the end of Plaintiff's Exhibit 15. Is it true that those ends are provided with two cut-out portions in the form of a leaf or a fern or some curvaceous element?

A. Yes, sir. Both exhibits show such a cut-out.

(Testimony of Bertram A. Kaepfel.)

The Court: By that you mean Exhibits 14 and 15?

The Witness: Yes, sir, both Exhibits 14 and 15.

Q. (By Mr. Miketta): And that is of different configuration than the zig-zag cut-outs on Exhibit 13; is that correct?

\* \* \*

The Witness: The answer is: Yes, it is.

Q. (By Mr. Miketta): Is it true, Mr. Kaepfel, that the end of Exhibit 15 is flat, it lies in a single plane, with the exception of certain recesses. There are two larger spaced recesses in the upper portion, separated by two smaller recesses, and then a lower recessed surface connected at its upper edge and extending from side to side at the end; is that correct?

A. That is a long sentence, but, to the best of my knowledge of the question, that is correct.

Q. Well, you were watching me while I was asking the question? [167]

A. Yes, sir, I was watching you.

Q. And you followed me, did you not?

A. Yes, sir.

Q. Of course, up above we have this knock-out, which in this instance has been knocked out and constitutes a hole?

A. Correct.

Q. And that end piece that you are looking at on Exhibit 15 is a casting, is it not?

A. It is a casting.

Q. Now, the end pieces of Plaintiff's device, Exhibit 13, are not a casting, they are pressings; is



(Testimony of Bertram A. Kaepfel.)

that correct?           A. They are stampings.

Q. Stampings—is that right?           A. Yes, sir.

Q. And the defendant's end piece has a two-tone effect in that the recesses which we have just described and identified have a pebbled surface, whereas the rest of that plane is relatively smooth; is that correct?

A. That is correct, yes, sir.

Q. Now, the end of Plaintiff's Exhibit 13, if we place the cover plate of the chassis into the recess of the end piece, and now consider both of them in the position which they would normally assume when hung, that end piece does not lie in a single plane, does it?

A. If you consider the entire end appearance as a single [168] element, it does not.

Q. Because the cover plate of the chassis protrudes beyond the plane of the lower portion; is that correct?           A. It is correct.

Q. Then, in addition to that, you do have a lower recess, which is trapezoidal in form somewhat, and that recess has the cut-out zig-zag pattern in it; is that correct?           A. Yes, sir.

Q. And that end of Exhibit 13 is one uniform texture of finish; is that correct?

A. That is correct, also.

\* \* \*

Q. (By Mr. Miketta): Mr. Kaepfel, will you please turn to Exhibit 2, and I will try to make this very brief. I understand that the tabulation of costs allegedly was made under your direction and some

(Testimony of Bertram A. Kaepfel.)

of it was made by you personally; [169] is that correct?

\* \* \*

The Witness: That is correct.

Q. (By Mr. Miketta): Did you personally check all of the invoices? A. Yes, sir.

Q. And you knew the dates of all the invoices?

A. Yes, sir.

Q. And the sums involved? A. Yes, sir.

Q. Now, on page 107, you were asked this question:

“And is the total sum shown by the summary on sheet A of Plaintiff’s Exhibit 2 for identification, being \$59,445.67, the amount actually paid by the plaintiff after the perfection of the design of the patents in suit . . . ?”

Were all those sums paid after you had perfected the design of the patents in suit?

A. Yes, sir. [170]

\* \* \*

Q. (By Mr. Miketta): I call your attention, Mr. Kaepfel, to Exhibit 2, sheet B, and I notice that the first four items there do not have a date other than 1944. That is correct, is it not?

A. It is difficult to see the marking. I believe I have it here now. The dates that you refer to in this place, in this instance, are the dates on which the orders were let for this die work, yes, sir.

Q. And the dates there appearing are simply the year 1944; is that correct? A. Yes, sir.

Q. You testified that you checked certain in-

(Testimony of Bertram A. Kaepfel.)

voices and knew the dates of the invoices. Why didn't you put those dates in?

A. Because at the time that I conceived the idea of keeping a running record of all these invoices, those had passed me by and were already in the company's file, but I had approved all of these invoices.

Q. Now, when did you start keeping this record?

A. I started keeping it, as near as I can remember, in December '45.

Q. December of '45?

A. No, no. That's wrong. But it must have been immediately subsequent to this, because all the other dates [172] are complete.

Q. They are? A. Yes, sir.

Q. I call your attention to sheet C in Exhibit 2,—— A. Oh.

Q. ——and particularly items 5 to 9, which simply bear the date 1945. What were the dates of those invoices?

A. The reason for the incompleteness of those dates is that in many instances I am asked to approve an invoice before I am given the original copy of the purchase order, which has the date on it, on which the original order is issued.

Q. Well, in other words, you didn't see the dates on those invoices, did you?

A. I see the date on the invoice, but not the date of the original purchase order. [173]

Q. Why didn't you put in the date of the invoice? I thought that is where you got your record.

(Testimony of Bertram A. Kaepfel.)

A. No, sir; I always put in the date that the original purchase order is issued.

\* \* \*

Q. (By Mr. Miketta): When did you get this compilation up?

A. The copies as you see them here were prepared for the purpose of this trial and would have been prepared within the last nine months.

Q. At that time when you were preparing this particular series of sheets, which are Exhibits 2-B to 2-F, did you check specified invoices against the figures which you now show here on Exhibits 2-B to 2-F?

A. No, sir, I did not check that personally. [174]

\* \* \*

Q. (By Mr. Miketta): Mr. Kaepfel, will you turn to Exhibit 2-M, the letter "M" as in Mary?

A. Yes, sir, I have it.

Q. That shows the one-piece side rail assembly, is that correct? A. Yes, sir, it does.

Q. Whereby you can punch one sheet of metal and have the top rail, the bottom rail, the ends, the three interconnecting members with their bosses?

A. Yes, sir.

Q. Now, with respect to that item M, which is identified on the drawing as S or PY-18468, I call your attention to Exhibit 2-C of your tabulation; now, the second item is S-18468, is that correct? That relates to Exhibit M.

A. Yes, sir, it does.

Q. And opposite that in the penultimate vertical



(Testimony of Bertram A. Kaepfel.)

column is 1755.57, is that correct?      A. Yes, sir.

Q. One thousand seven hundred fifty-five dollars and fifty-seven cents. Now, will you look at the ninth item?      A. Yes, sir.

Q. Does that relate to the same device?

A. Yes, sir, it does.

Q. And what figure is charged against that?

A. \$160.60.

Q. Now, look at the eleventh item. Is that the same device?      A. Yes, sir, it is.

Q. And how much is charged against that?

A. \$810.

Q. Now, look at the fifteenth item. Is that the same piece?      A. Yes, sir, it is.

Q. How much is charged against it? [177]

A. \$1,755.57.

Q. How is it that you have charged upon this thing, under the date of 1944 in the second item on that page, exactly the same figure of \$1,755.57, and then repeated that under the date of 9-25-44 in item 15?

A. That can be due only to a clerical error on the part of the stenographer tabulating this sheet.

Q. Would it surprise you to know, Mr. Kaepfel, that there are a number of similar duplications here?      A. It would, yes, sir.

Q. Shall I prove it to you?      A. Sir?

Q. Shall I prove it to you?

The Court: Counsel for the plaintiff concedes that it is a complete list of all parts of the device. By that it would include the can, for instance. [178]

Mr. Foster: Yes, sir.

(Testimony of Bertram A. Kaepfel.)

The Court: Which obviously isn't part of the design patent. It apparently includes anything that concerned this device, and it has been broken down.

With that concession, of course, it means that if there was any issues of the amount of money that pertained to this design, somebody would have to go through and segregate it. I am not. As far as I am concerned, you needn't have any concern. I am merely assuming that money was spent and work was done on the device. Now, as to what an appellate court might do about it, I don't know.

I think in view of your cross-examination and in view of your statement in the record that there are matters here that are not attributable to the matter of the design, and in view of the statement of this court, I don't think you need be concerned about your record. This isn't an accounting procedure. I admitted it only because it showed money had been spent, work had been done. I attempted to get you gentlemen to stipulate just in those words, in which event I was going to exclude it, because that is as far as I am going to consider it. [179]

\* \* \*

The Court: I don't think you object to the position I am taking.

Mr. Foster: No, sir, I raise no objection. [180]

\* \* \*

Q. (By Mr. Miketta): Mr. Kaepfel, will you examine the side of plaintiff's Exhibit 15. That side is composed of an upper rail and a lower rail; is that correct?      A. Yes, sir, it is.

(Testimony of Bertram A. Kaepfel.)

Q. Are there three integral parallel bars connecting the top and bottom rail?

A. There is one of them which connects the two rails. The other two are adjacent and appended to the center rail.

Q. You are referring to this medallion?

A. Yes, sir.

Q. That is located midway of the ends of the entire side panel?      A. Yes, sir. [181]

Q. Is that medallion integral with the top and bottom rails, or has it been appliqued or welded on?

A. It has been applied.

\* \* \*

#### Redirect Examination

By Mr. Foster:

Q. Mr. Kaepfel, reference was made to Plaintiff's Exhibit 2 in your cross examination, and the fact there was a duplication of one of the items that went into the final summary that appears in that exhibit. Have you carefully checked, in response to my request, the compilations which appear in Plaintiff's Exhibit 2 during the noon recess?

A. Yes, sir; I have checked those figures.

Q. And is my understanding correct that you have found that there are two duplications and one instance of a transposition of the figures?

A. Yes, sir; that is so.

Q. And that causes the total which appears upon the sheet A of Plaintiff's Exhibit 2 to be changed from \$59,445.67 to \$57,238.12; is that correct?

(Testimony of Bertram A. Kaepfel.)

A. Yes, sir; that is correct.

Q. And it causes the second amount from the top on the same sheet to be changed to \$23,626.75, and the fourth [182] item from the top of that page to be changed to \$9,457.98; is that correct?

A. Yes, sir, it does.

Q. That would involve also those same amounts that are reflected on Page C, and would involve the striking out of the 12th and 15th horizontal row of figures because they are duplications of others?

A. Yes, sir; that is correct.

Q. Are there any other corrections to be made in the compilations which are in Plaintiff's Exhibit 2?

A. No, sir; there were no other corrections.

Q. And where those changes occur or should be made, those are the compilations made by the stenographic help in your office, under your general supervision; is that correct?

A. Yes, sir; that is so.

Mr. Foster: Permission is asked of the court to make the changes I have indicated, which appear in the record and which have been testified to by Mr. Kaepfel, in the original court's copy, and we will gladly identify them to counsel, if they haven't taken notes of the corrections.

The Court: It may be done.

Mr. Foster: Thank you, sir.

The Court: Counsel will make the necessary corrections. I put them in in pencil, but you may correct them. [183]



(Testimony of Bertram A. Kaepfel.)

Mr. Foster: Thank you, sir.

Q. (By Mr. Foster): During your cross-examination, as I recall your testimony, it was that you embarked upon this work of developing the designs of the fixtures of the patents in suit and had authority to have the mock-ups made of the various stages of that design given to the shop. Did Mr. Biller have anything to do with the commencement of the work upon development of the patented design, or authorizing or directing the shop to make the mock-ups?

A. Yes, all that work was done with Mr. Biller's full knowledge, and with his consent. [184]

\* \* \*

Q. On cross-examination you testified that you had the desire to develop a new design of lighting fixture which led to the design of fixtures shown in the patent in suit, and Mr. Biller knew of that desire on your part, did he not?

A. Yes, sir, he knew of it very shortly after the thought occurred.

Q. You say that he knew of it. You know that by virtue of your conversations with him, is that correct?

A. Yes, sir, because I made sketches and at the very first opportunity discussed that matter with him as to the——

Q. How soon after your first discussion of this desire did Mr. Biller participate with you in making

(Testimony of Bertram A. Kaepfel.)

designs for a fixture preliminary to the design of the fixture of the two patents in suit?

\* \* \*

The witness: The answer to that would be that it would be at the very first good opportunity. It might have been one week, it might have been two weeks after I had some preliminary sketches that I would have been able to talk to Mr. Biller about it.

Q. (By Mr. Foster): Thank you, Mr. Kaepfel. In your cross examination now you referred to an angle which I think [186] you called the cut-off angle, as having some effect upon the number of transverse louvers in an overhead lighting fixture for a fluorescent tube. What is that cut-off angle?

A. That cut-off angle would be the angle described between a horizontal plane and an oblique plane running from the bottom of one louver across the top of the other, of the next adjacent louver.

Q. If my understanding is correct, the cut-off angle, then, is the angle between the horizontal plane and the plane of observation of an observer, along which latter plane he could look beneath the edge of one transverse louver and above the edge of the adjacent louver and see the fluorescent tube, is that correct? A. Yes, sir, that is correct.

Q. Does the depth or height of the transverse louver, as well as this cut-off angle, affect the number of transverse louvers that one could have in a given length of light fixture?

A. Yes, sir, every element is effected there.

(Testimony of Bertram A. Kaepfel.)

Q. So if we change either the depth of the transverse louvers or we change the cut-off angle that we desire for a given length of light fixture, we will change the number of transverse baffles, is that correct?      A. That is correct.

The Court: When you change the depth of a louver, you [187] automatically change the cut-off angle, don't you?

The Witness: Yes, sir, every element is subject to alteration there.

Q. (By Mr. Foster): But is there anything critical or fixed in that cut-off angle that you must work to? In other words, must you always have that cut-off angle of a given value in different fixtures?

A. Not necessarily at all.

Q. Do you remember what the cut-off angle is approximately in the Viz-Aid fixture, Plaintiff's Exhibit 13?

A. As it now is? I believe it is 28 degrees.

Q. Would the utility of that fixture in your opinion be destroyed if the cut-off angle were made of a different value, a different number of degrees?

A. No, sir, not in the least.

Q. Could a usable fixture be provided if the cut-off angle were 25 degrees instead of 28?

A. It could.

Q. Or 35 degrees instead of 28?

A. It could.

Q. Or any number of degrees differing by one between 25 and 35?      A. It could.

Q. Is there anything critical in the height or

(Testimony of Bertram A. Kaepfel.)

depth of the transverse louvers in this Viz-Aid fixture, Plaintiff's [188] Exhibit 13?

A. No, sir, there is not.

Q. Do you recall any vertical dimension of those louvers? A. No, sir, I do not.

Q. Could they be made  $\frac{3}{4}$  of an inch greater in depth or height or  $\frac{3}{4}$  of an inch less and still be a usable fixture? A. They could, yes.

Q. They could be made to vary as much as an inch in their vertical dimension from their present vertical dimension, or any dimension in between those two limits that I have arbitrarily picked out, varying, say, an eighth of an inch from each other?

A. That they could.

Q. So if we allowed ourselves, as you say we might and still have a usable fixture, we could have eight different variations of height in the transverse louvers differing from each other an eighth of an inch and still have a usable fixture, is that correct?

A. That is true.

Q. And we would still have a usable fixture if we varied the cut-off angle in increments of one degree 10 times, 10 different values between 25 and 35 degrees, and still have a usable fixture? [189]

A. That is true.

Q. And both those variants would affect the number of transverse louvers we would have in a given length of fixture? A. Both of them would.

Q. Is there anything critical in the number of transverse louvers, numbering 13, that are employed in the plaintiff's fixture Plaintiff's Exhibit 13?



(Testimony of Bertram A. Kaepfel.)

A. No, sir, there is not.

Q. Would a usable fixture in your opinion have been provided by one having eight or nine transverse louvers?      A. Yes, sir.

Q. Or 16 or 18 or 20 transverse louvers?

A. Yes, sir, it would have.

Q. Or any number in between those limits I have arbitrarily chosen, is that true?

A. Any number, yes, sir.

Q. Aside from the fact that the overall length of a fixture such as Plaintiff's Exhibit 13 must be sufficient to accommodate a 48-inch tube within it, is there any limit to the length, overall length of the fixture?

A. No, sir, there would be no maximum limit. There would be only a minimum.

Q. The fixture could be made longer than it is by as much as an inch or two inches or three inches and still have a [190] usable fixture, one of utility?

A. Yes, sir, even more than that.

Q. And it could be varied in increments of 1/16 or 1/8 of an inch or 3/16 up to several inches longer than it is now and still have a usable fixture?

A. Yes, sir.

Q. So if we varied it over a two-inch limit, its length of increments of a sixteenth of an inch, we would have 32 possible variants or overall lengths of fixture that we could employ and have a usable fixture of the type of Plaintiff's Exhibit 13?

A. That is true.

(Testimony of Bertram A. Kaepfel.)

Recross Examination

By Mr. Miketta:

Q. Mr. Kaepfel, did I hear you correctly in stating that there is no limit to the maximum length that the fixture can have, assuming that it originally was supposed to receive a 48-inch tube?

A. Well, that would be true aesthetically. Economically, perhaps not. There is a limit to the length of a piece of steel, and that would be the limitation on the length of a fixture.

Q. I think you said you could easily make [191] this four or six inches longer. Could you make it two feet longer?

A. If it were desired, yes, sir, it could.

Q. And all you are interested in, of course, in view of the experience that you have had in tool making, is the aesthetic appeal, is that right?

A. In a fixture of this type, yes, sir. [192]

Q. And if you were to put, let us say, a 48-inch tube in a fixture that is 6 feet long, and you put those fixtures in an adjacent aligned relationship, then you think you will have uniform lighting; is that correct?

A. Not necessarily, no, sir.

Q. In other words, there is a limit to the length of the fixture, if you want efficient lighting?

A. If you want uniform lighting, then the statement is true, yes, sir.

Q. Now, you spoke of the various spacings between transverse baffles and various cut-off angles,

(Testimony of Bertram A. Kaepfel.)

and the effect of changing the height of the transverse baffle, its effect on the cut-off angle, and so forth. All those variables were known before 1942, weren't they?      A. Oh, yes, no doubt.

Mr. Miketta: That is right. Thank you.

The Court: In the lighting industry have these units of lighting fixtures that take a 4-foot tube been fairly well standardized? For instance, take a factory or a work room with these lighting fixtures holding fluorescent tubes in a series, and if the owner of the building wanted to remove one and put in another one, has the size been fairly well standardized in the lighting industry, or what is the variation you find in the lighting industry, if you know, on [193] fixtures which hold a 4-foot tube?

The Witness: If I understand your Honor correctly, the answer would be that each individual manufacturer establishes his own standard in that respect, and that standard varies also as to whether the fixture is ornamental or whether it is purely a functional fixture for factory or industrial lighting. If I may elaborate on that, we have industrial lighting which runs  $52\frac{3}{4}$  inches long for a 48-inch lamp. That is the standard that we established, but that was for industrial purposes only.

The Court: Does that correspond with a similar length on the part of other manufacturers for industrial purposes?

The Witness: To the best of my knowledge, it does not.

The Court: All right. [194]

\* \* \*

PROFESSOR ROBERT L. DAUGHERTY  
called as a witness by and on behalf of the plaintiff,  
having been first duly sworn, was examined and  
testified as follows:

The Clerk: Take the stand. What is your name,  
please?

Direct Examination

The Witness: Robert L. Daugherty.

By Mr. Foster:

Q. Would you state your residence, and your  
age, please, Professor?

A. I live in Pasadena, California, and I am  
sixty-four years of age.

Q. You are a professor at the California Insti-  
tute of Technology in Pasadena; is that correct?

A. I am.

Mr. Foster: Your Honor, I have had the priv-  
ilege of examining Professor Daugherty as an ex-  
pert, and I think it would save some time and also  
avoid any impairment of his sense of modesty if I  
read from another record what I know to be his  
qualifications. May I do that?

Mr. Miketta: We will accept that.

The Court: That is satisfactory.

Q. (By Mr. Foster): I understand, Professor,  
that you have graduated in Mechanical Engineer-  
ing from Stanford University in 1909; that you



(Testimony of Robert L. Daugherty.)

were an instructor in Mechanical Engineering Laboratory at Stanford in 1909 and '10; that [195] you were Assistant Professor of Hydraulics at Cornell University from 1910 to 1916; Professor of Hydraulic Engineering, Rensselaer Polytechnic Institute from 1916 to 1919—that is spelled R-e-n-s-s-e-l-a-e-r, and I understand that even some graduates from that university cannot spell it; that you were Professor of Mechanical and Hydraulic Engineering and head of the Mechanical Engineering Department of the California Institute of Technology since 1919;

That you are a Fellow and past Vice-president of the American Society of Mechanical Engineers; Regional Advisor of the Engineering, Science and Management War Training, U. S. Office of Education for Southern California, Arizona, and New Mexico, and Western Texas from 1940 to 1945;

That you are the author of numerous books, including Hydraulic Turbines, published three times; Centrifugal Pumps; and Hydraulics, published four times, and that your books are used as texts in most engineering colleges, including Cal. Tech.;

That you are author of a section on "Pumps, Compressors, and Hydraulic Turbines" in "General Engineering Handbook," published in 1932 and 1940; that you are author of the textbook for the International Correspondence Schools on "Water Turbines;" and author of numerous technical papers;

That you were retained in a consulting capacity

(Testimony of Robert L. Daugherty.)

with the Metropolitan Water District on Pumps for the Colorado [196] River Aqueduct in 1933 to 1936; that you have been consultant with the United States Bureau of Reclamation on pumps for the Grand Coulee project on the Columbia River from 1938-40 and 1946-47; and consultant for the Denver & Rio Grande Railroad on ventilation of the Moffat Tunnel, which is the longest tunnel in the world using steam locomotives; that you are consultant for the Union Oil Company, Riverside Cement Company, Goulds Pumps of Seneca Falls, New York; General Petroleum Corporation, and many others, and chairman of the Advisory Committee to the Board of Directors of the Air Pollution Control District here. Is that all true, and are you that Professor Daugherty?

A. Yes, sir. That is the record. [197]

The Court: Did you ever write a book on the laws of chance?

The Witness: No, I didn't write such a book.

Q. (By Mr. Foster): But did you make any calculations in response to a request from me, Professor, on the laws of chance as applied to a determination mathematically on whether if we had five, six, seven, eight, or nine dimensions or numerical values, and with respect to each one we had only two possibilities, one, a possibility of making that dimension a given value, and, two, a possibility of making it just one other value, and determine what the mathematical possibility of our having eight dimensions identical would be, that is, if we had

(Testimony of Robert L. Daugherty.)

eight dimensions of two different designers of a lighting fixture, for example, which were identical, and we had only two possibilities for each dimension, what is the probability of that being coincidental?

A. Yes, I have made such a calculation.

Q. Would you explain what the calculation or the formula for it involves, and in that regard if you would like to approach the blackboard and show us what is to be done, will you please [198] do so?

\* \* \*

The Witness: The mathematical calculation of probability and chance is very simple, and one about which there is no question, but I think it might be helpful if I would illustrate it by a very simple example.

Suppose that in a bag, we will say, there was one white ball and one black ball, and that a person were just to reach in the bag and to pick out any ball. The chances that it would be the white one would be one out of two. If in another bag there were three white balls and seven black balls, and again at random one were to pick out a ball, the chances that it would be a white ball would be three out of ten. If in a third bag there were two white balls and twelve black ones, the chances you would pick out at random a white ball would be two out of fourteen.

Now, if at random one were to reach his hand

(Testimony of Robert L. Daugherty.)

in each one of these bags and pick out a ball, the chances of all of them being a white ball would be obtained by multiplying these numbers together, and the answer is six divided by 280. That is, the chances of picking out three white balls at random out of the three bags would be six out of 280. And that is the only principle that is involved in all of these other subsequent calculations.

Mr. Foster: Thank you, sir.

Q. (By Mr. Foster): Now, I have here, Professor Daugherty, and it is before the court, the two-and-one-half page report on your stationery which you gave me day before yesterday, that is marked tab J of Plaintiff's Exhibit 11. I show you a copy of it, and is that two-and-one-half-page report one prepared by you.

A. Yes, that was prepared by me.

Q. Are the mathematics in that report correct?

A. They are.

Q. What figure did you get, assuming that we had eight identical dimensions in two different devices and assuming with those eight dimensions that each of them had only two possible values, one, the value that the dimension actually was given in the device, and, two, just one other possible value, what was the probability of two devices having the eight dimensions identical being coincidental? [200]

A. That would be your first number on the board, one-half multiplied by itself eight times, and the answer would then be 256; that is, there is one chance



(Testimony of Robert L. Daugherty.)

in 256 that all eight dimensions would be identical if there were only two choices for each one.

Q. Now, in this report, Professor, assuming that the smallest—or, suppose that one of those numbers, one of those eight could be any one of fifteen possible variations, and suppose we had nine dimensions that are identical, and each of the eight other dimensions could be only one of two possible dimensions, again. What would be the probability of the nine dimensions being identical in two devices, being coincidental or accidental?

A. Well, in those calculations the first fraction would be one over 15. The other would be one over 2, and that multiplied by this eight times, and that would be one chance in 3,840.

The Court: How do you arrive at the 15 to start with?

The Witness: Well, that was just a mere assumption that in one case in this case the number of louvers, which happens to be 13, might be either a greater or a smaller number than that. And, of course, as soon as I get beyond this one to two, I have to make some kind of an assumption. One is, which I made here, that there could be at least three and at most seventeen, and, to have the chance [201] that it would be thirteen louvers instead of anything between three and seventeen would be just one chance in fifteen. For all of the rest of them I still stuck to the first assumption, that it was either the one dimension or some other dimension.

(Testimony of Robert L. Daugherty.)

Mr. Foster: Does that answer your Honor's question?

The Court: Well, it answers it, although I still don't know exactly how the figure 15 comes into it. That is figured out by some other formula?

The Witness: No. You see, if there could be three louvers, or four, five, six, seven or eight, on up to seventeen——

The Court: There would be fifteen possibilities.

The Witness: ——fifteen possibilities, and there would be only one out of fifteen that it would be thirteen. That is how it was arrived at.

Q. (By Mr. Foster): So that, as I understand you, Professor, if we have eight dimensions which are identical, and we assume that those dimensions, each of them, has only one possibility that it can be the value it is or only one other value, then our formula for determining what is the probability of the two devices having the eight dimensions identical is one-half times itself eight times?

A. That is correct. [202]

Q. And if any one of those dimensions could have been not one out of two possibilities, but one out of eight possibilities, we would then substitute for one of the one-halves in the formula, one over eight?

A. That's right.

Q. And multiply it by one-half the remainder of the times or seven times to get that probability?

A. That is correct.

Q. And if another of the dimensions could have been any one of 15 possibilities instead of two pos-

(Testimony of Robert L. Daugherty.)

sibilities, we would substitute in the formula for one over two on one occurrence one over 15?

A. That is correct.

Q. And that would give us the mathematical chance of the identity of the two devices being accidental or coincidental, is that correct?

A. That is correct.

Q. Then I notice that in your report on page 2 you have assumed at the bottom of page 2 possible variations, and you got seven possible values that could have been chosen for one of these items and then determine the probability from that, and I notice on page 3 you have extended the same line of reasoning to the remaining five dimensions and there you have made the assumption that there are seven possible values that could have been selected for seven of the dimensions, 15 [203] possible values that could have been chosen for one and only two possible values that could have been chosen for another, the last one? A. That's right.

Q. And determined that the chance of the nine dimensions or measurements being identical in two devices, being coincidental or accidental, is one out of 24,706,290, is that mathematically correct?

A. That is the correct figure.

Q. I call your attention to the fact, Professor, that listed in this Plaintiff's Exhibit 11 in the next lettered tab K there is a title which I wish to call to your attention, "Some Identities of Patented and Accused Designs," and that lists 24 items. Have you calculated what the chance is of two devices being

(Testimony of Robert L. Daugherty.)

identical in 24 dimensions or respects, assuming that as regards to each there are only two possibilities of the dimension having a value, that is, one the value it has, and, two, some other value, but only two possibilities?

A. That is correct, I have made such calculation.

Q. What does that calculation show as the probability, or I should say improbability—what is the chance of two features being identical in 24 respects under that assumption?

A. For 24 different respects where there are only two [204] possibilities for each one of the 24, the chance is one in 16,777,216 that they will be identical in all 24 respects.

Q. One other question, Professor. I direct your attention to a light fixture here, which is Plaintiff's Exhibit No. 15, and wish you to observe only its general shape, the kind of device it is, it is for lighting with fluorescent tubes, as you can obviously see. If I told you that as regards the dimensions and angles of the edges of the end of that fixture and its overall length and height and location of a decorative piece on its sides there were eight or nine respects in which that fixture was identical with a fixture for the same purpose, but manufactured by a different company, would it be your opinion, based upon your years of experience in design work both in teaching and making designs that such identities were accidental or coincidental?

A. I don't see how they could possibly be accidental.



(Testimony of Robert L. Daugherty.)

Mr. Foster: The report of Professor Daugherty which he has identified and which is tabbed, the two and a half, three pages of it, tabbed I of Plaintiff's Exhibit 11, is offered in evidence at this time.

The Witness: Isn't it G?

Mr. Foster: It is tab J.

The Court: It may be received in evidence. [205]

\* \* \*

Mr. Foster: I would like to also offer as Plaintiff's Exhibit next in order, your Honor, the enlarged chart, which is merely an enlargement of the print which is found in Plaintiff's Exhibit 11 as tab I.

In case there is an appeal here, reference could be made to it before the Appellate Court.

The Court: 11-I is already in evidence.

Mr. Foster: I would like to offer the enlargement for reference purposes.

The Court: All right.

The Clerk: Plaintiff's Exhibit No. 16.

\* \* \*

Q. With further reference to the fixture, Professor, to which I directed your attention, Plaintiff's Exhibit 15, I show you Plaintiff's Exhibit 16, which is an outline in solid lines of the end plate of the fixture design, and in dotted lines the outline of the end plate of a similar fixture manufactured by a different company, and state to you that in both of these fixtures the number of transverse louvers is

(Testimony of Robert L. Daugherty.)

13, and in both of them the overall length is 48-7/16 inches, and call your attention to the fact that these outlines, the [206] solid line outline and the dotted or broken line outline not only are almost identical, but that the angle relationships and dimensions indicated in 1, 2, 3, 4, 5 places are identical, and that not indicated by any arrow, but nevertheless a fact, is the vertical sidewalls upon the upwardly projecting portion of the top in each device, and ask you based upon your years of experience in teaching design and designing devices whether it is your opinion that such identities of angles and dimensions and number of louvers and lengths is likely to be coincidental or accidental?

A. No, I don't think it is probable.

Mr. Foster: That is all.

### Cross-Examination

By Mr. Miketta:

Q. Professor Daugherty, I feel very much at a loss cross examining on a subject such as this form of mathematics, but may I approach it from this standpoint? Have you made a study of lighting fixtures, Professor? A. I have not.

Q. In other words, you are approaching this from a purely mathematical standpoint?

A. Absolutely.

Q. And your opinion is based upon the assumption that certain facts and figures which have been presented to you are correct? [207]

(Testimony of Robert L. Daugherty.)

A. That is true.

Q. We will get along very much better because now we can talk the same language.

There may have been in the past, and I say "may" and if you were to assume that in the past there have been lighting fixtures of similar contour and of similar sizes, then your mathematics are just as correct as if there had never appeared previously fixtures of the same size and of the same contour, isn't that correct?

A. I believe that is true, if I understand your question.

Q. In other words, your mathematical computations do not take into consideration the possibility, let us say, that in the past, say back in 1942, fixtures were in existence that had the same contours or cross-sections and substantially the same angles as indicated on Exhibit 16.

A. No, I have made no study of the prior art, not even of the patents in this particular case. I have just simply calculated by laws of probability and chance what these possibilities are that have been submitted to me.

Q. I think you have been very wise to keep away from the patents or I would have cross examined you on that, because those I know.

Isn't it true in this example that you have given about the white marbles and the black marbles that there is a defect [208] in that method inherently, because suppose the black marbles are lots heavier than the white marbles.

(Testimony of Robert L. Daugherty.)

A. Well, that wasn't part of the assumption at all.

Q. But assuming that they were.

A. If that were the case one might tell by feeling that there was a difference. If a man were blind-folded, for example, and he picked up one, he couldn't tell in any way. This is just a mere chance.

Q. I am saying if the black ones were square or heavier than the white ones.

A. That takes out all elements of chance if some were square and some were round.

Q. That takes out the element of chance and, therefore, if some of those possibilities, let's call them, instead of marbles, are not only of unequal value but by reason of their utilitarian function they are very important, then of course the mathematical equation which you have used, the mathematical method which you have used, is not applicable, is that correct?

A. That may be true. That, of course, however, is not my problem in this case.

Q. No. All I know about this subject, Professor, I have learned by reading your report, the Encyclopedia Britannica, and one work on the law of chance and probabilities. But this heavy marble business is one that stuck in my mind, [209] because even I can understand that.

You were supplied with all this information, were you not? A. Correct.

Q. Did you make any of these measurements yourself? A. I did not.



(Testimony of Robert L. Daugherty.)

Q. You are not responsible if, for example, Exhibit 16 is slightly in error? A. No.

Q. Very well. You do state on page 2 of your report, "The bottom of the two fixtures is a V-shape with an angle from the horizontal of  $7\frac{1}{2}$  degrees."

Did you actually measure the angle?

A. No. I was supplied with that information. I could see that it was V-shaped.

Q. But that angle you did not measure yourself?

A. No, I didn't. I didn't measure anything. I just simply observed the drawing, such as the one that is in evidence down here as Exhibit 16. That is what was shown to me.

Q. Professor, you have probably seen during your stay in the court room the two end portions of the plaintiff's device and of the defendant's device, and I am referring to Exhibits 13 and 15; can you observe a difference in the formation of the design appearing on those two end portions? [210]

\* \* \*

The Witness: Yes, I observe a difference in the appearance of the ornamental features, if that is what you have in mind.

Mr. Miketta: Yes, Professor.

Q. Can you express mathematically the number of variations which could exist between the design appearing on Exhibit 13 and the design which appears on Exhibit 15?

A. As far as that appearance is concerned, do you mean?

(Testimony of Robert L. Daugherty.)

Q. Yes, how many variations could exist between what is shown on Exhibit 13 and what appears here?

Mr. Foster: That is objected to as being ambiguous. I don't understand it at all. But if the witness does, he can answer it.

The Witness: I think there can be an indefinite number of variations in those little details of the ornamentation.

Q. (By Mr. Miketta): Not only indefinite, but almost infinite?

A. Yes. Of course, my calculations were on more or less definite physical measurements that were given to me.

Q. And if the number of variations is infinite, then of course the chance of duplicating them is also infinite isn't that right?

A. One in infinity.

Mr. Miketta: Thank you very much. [212]

\* \* \*

### LOUIS J. ROZIER

called as a witness by and on behalf of the plaintiff, having been first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Foster:

Q. State your full name, please.

A. Louis J. Rozier.

Q. Your residence, please?

A. Kirkwood, Missouri.

(Testimony of Louis J. Rozier.)

Q. Are you an employee of the plaintiff, the Day-Brite Lighting, Inc.?      A. I am.

Q. How long have you been employed by the plaintiff?      A. Since August of 1937.

Q. In what capacity are you employed?

A. Advertising and sales promotion manager.

Q. Do you have anything to do with the contact work with advertising agencies which prepare the copy for advertisements of the plaintiff's products?

A. It is my responsibility.

Q. Do you have anything to do with the literature, price lists, bulletins, printed for Day-Brite with respect to [214] the lighting fixtures it makes and sells?

A. I create them and supervise their production.

Q. Do you have anything to do with the art work that is used in the literature and advertisements of lighting fixtures of the plaintiff?

A. I supervise its production.

Q. What is the size of the department you supervise?

A. It includes an assistant, a secretary, two artists and two clerks and myself.

Q. With regard to the creative work of advertising and exploitation, and the creation and maintenance of a market for the Viz-Aid patented design fixture by Day-Brite, the plaintiff, have you had anything to do with that?

(Testimony of Louis J. Rozier.)

The witness: Yes, sir, everything that had to do with the advertising and promotional end of it.

Q. (By Mr. Foster): Are the records which show the expenditures made in the advertising of the Viz-Aid fixture, Plaintiff's Exhibit 13, in your custody in your department?

A. The figures on the advertising have passed through my department, yes.

Q. And have you prepared, in response to my request, any summary of the literature costs and advertising of plaintiff's [215] fixture marked Plaintiff's Exhibit 13?

A. I have.

Q. I show you a volume marked Plaintiff's Exhibit 6 for identification and ask you if that is what you had reference to in your last answer?

A. Yes, this is the book that I prepared or supervised the preparation of.

Q. The one that I have handed you is the court's copy. I will return it to the clerk and ask you to direct your attention to my copy of that book. I notice that there are tabbed in it a number of separate sheets. Will you direct your attention to tab A and explain what is there shown?

A. Tab A contains a summary of Viz-Aid advertising costs itemized by agency expenses through 1945, '46, '47, '48 and part of '49, plus the literature printing costs for the Viz-Aid advertising material, totaling in excess of \$88,000.

Q. And tab B of Plaintiff's Exhibit 6, what is there shown?



(Testimony of Louis J. Rozier.)

The Court: Counsel, you are talking about Viz-Aid. Is there any stipulation that this light fixture, Plaintiff's Exhibit 13, is the Viz-Aid light?

Mr. Foster: There is no stipulation on that as yet.

Do you so stipulate, that Viz-Aid is the Plaintiff's Exhibit 13, Mr. Miketta. I have here all the [216] bulletins.

Mr. Miketta: It is my understanding, your Honor, that the plaintiff corporation has called this fixture of theirs, Exhibit 13, by the trade name Viz-Aid, and I think I will accept the witness' statement to that effect.

Q. (By Mr. Foster): That is true, isn't it?

A. That is true. It is a registered trademark.

Q. For the lighting fixture Plaintiff's Exhibit 13 which you have seen here in court, is that correct? A. That is correct. [217]

\* \* \*

Directing your attention to tab B entitled "Viz-Aid Literature Costs," in Plaintiff's Exhibit 6, what is there shown?

A. That is a breakdown of the cost of the individual bulletins that have been published promoting the sales of the Viz-Aid.

Q. Those individual bulletins are then bound in this Plaintiff's Exhibit 6 and tabbed as I, J, K, L, M and N, is that correct? A. That is correct.

Q. And each of these bulletins that I have last referred to depicts and advertises only the Viz-Aid

(Testimony of Louis J. Rozier.)

and Topnotch—principally Viz-Aid lighting fixture like Plaintiff's Exhibit 13?

A. Principally, yes.

Q. Each of these bulletins that I have referred to has also, appearing on the lower left-hand corner of its back cover, the approximate date of printing and distribution, and the number of copies of each bulletin which were made?

A. In some place in the bulletin, not always the same positions. [220]

Q. Some places it occurs inside the front cover at the lower left?

A. That is correct.

Q. In one place or another it shows that 50,000, or whatever the number was, was distributed?

A. That is correct.

Q. And the cost of these bulletins is what you have set forth on sheet B of Plaintiff's Exhibit 6; is that correct?

A. That is correct.

Q. And all of those literature costs total \$9,600.71, as shown on sheet A of Exhibit 6?

A. That is correct.

Q. Turning now to sheets which are marked O, AA, AB, and through AS, there is listed for each year the amounts paid for advertising space and production to the agencies named upon that sheet, for advertising of the Viz-aid lighting fixture by the plaintiff, like Plaintiff's Exhibit 13; is that correct?

A. That is correct.

(Testimony of Louis J. Rozier.)

Q. And that amount is summarized upon sheet A of Plaintiff's Exhibit 6 in that total; is that correct? A. That is correct; yes, sir.

Q. And those figures and compilations upon the sheets I have referred to you have checked from the records [221] ordinarily kept and passing through your hands and in your custody at the company; is that correct?

A. That is correct.

Q. Would you explain the nature of the records from which these compilations were made?

A. The court's copy contains typical purchase orders and invoices covering the production of various ads and tear sheets of the ads in those cases follow these typical invoices. The space cost in the publication can be picked up from the agency invoices, as typical of what these costs are. The space costs are available. Anyone can find them through the Standard Rate and Data Service, and, of course, the space costs are published and are the same to everyone. It is billed to everyone through the agency.

Q. And those records you have identified were used, therefore, in checking the accuracy of this figure of \$88,046.73 on tab A of Plaintiff's Exhibit 6? A. Correct.

Q. And that is the expenditure made by the plaintiff for the years 1945 through the first three months of 1949? A. That is right.

Q. In advertising its Viz-aid lighting fixture, Plaintiff's Exhibit 13; is that correct?

(Testimony of Louis J. Rozier.)

A. Correct; yes, sir.

Q. Now, I wish to show you—— [222]

The Court: Just a moment. Do I understand that was all spent just in advertising this one fixture, the 48-inch fixture, with—what is it?

The Witness: Two tubes.

The Court: ——two tubes?

The Witness: That is correct.

The Court: And other amounts were spent by your company for advertising 18-inch, 24-inch, and 36-inch fixtures?

The Witness: Not as such. Other amounts were spent by the company for advertising other fixtures of 48-inch and 60-inch size. The 18, 24 and 36-inch lamps are strictly general. So far as promotion and advertising, they are cataloged, but they are not picked for advertising.

The Court: Then you had a cost distribution system so as to apportion to the various fixtures that you put out the particular costs of advertising, so that you could allocate to this particular fixture which is Plaintiff's Exhibit 13 in evidence the cost to that fixture?

The Witness: It wasn't done actually on an allocation basis, but these costs summarized were pulled from the tear sheets of the advertisements. You will see later in another exhibit—you will see in two later volumes that those ads were devoted exclusively to the Viz-aid fixture.



(Testimony of Louis J. Rozier.)

The Court: What do you mean, the Viz-aid [223] fixture?

The Witness: That is the two-lamp 48-inch, until the two 100-watt fixture was announced of the same design. I believe some of those ads will indicate in them specifically the amount where it was two 40-watts, or 100 watts, or whatever it was.

Q. (By Mr. Foster): Is my understanding correct, referring to this tab A of Plaintiff's Exhibit 6—— A. That is B.

Q. ——that the agency costs that are listed there related to the tear sheets which appear in the volumes marked Plaintiff's Exhibits 7 and 8, for identification? A. That is correct.

Q. And the amounts expended, as shown, to the agencies on that tab sheet A of Plaintiff's Exhibit 6 were for the advertisements represented by the tear sheets in the two volumes, Plaintiff's Exhibit 7 and 8, for identification?

A. That is correct.

Q. Where did these tear sheets in Plaintiff's Exhibits 7 and 8, for identification, come from?

A. They came from my office records or scrap-books that we try to keep of all of the publications in which we advertise. We don't catch them all, but we catch all that come over our desks where we normally receive tear sheets.

Q. I notice that many of the tear sheets have the name of the magazine and the month and year of

(Testimony of Louis J. Rozier.)

the publication, [224] and that those that do not have some pencil notation on the margin, or ink notation. Who places the notation in handwriting upon the tear sheets?

A. Whoever is clipping the ads in the department. Those are not mine, particularly. That is the clerical help that clips the magazines as they come through.

Q. But the longhand notations on the tear sheets in these volumes, which are Exhibits 7 and 8, for identification, are put on in your department?

A. That is correct.

Q. And they are made pursuant to your direction, that they should do so?

A. That is correct.

Q. And the tear sheets are kept in your department pursuant to your instructions and directions?

A. That is right.

Q. And you bound these tear sheets, taking them from your office, into these volumes, Plaintiff's Exhibits 7 and 8, for identification?

A. That's right.

Q. To the best of your knowledge, except for the pencil or ink longhand notations indicating the title of the magazine and the day and month of the publication, are these tear sheets all in the exact form in which they were published in the magazines identified on them, in the month and year [225] indicated thereon?

A. That's correct.

Mr. Foster: The two volumes identified by the witness, marked Plaintiff's Exhibits 7 and 8, for

(Testimony of Louis J. Rozier.)

identification, are offered in evidence as Plaintiff's Exhibits of the same number, your Honor.

The Court: They will be received in evidence.

\* \* \*

Q. (By Mr. Foster): Now, I direct your attention, Mr. Rozier, to tab AY of Plaintiff's Exhibit 6, for identification, and ask you what is there set forth.

A. That is a summary of Viz-aid sales from the beginning in 1945 through the first three months of 1949. The national figures are given in units and dollar value in the [226] first two columns, following the year date. The California sales in units and dollar value are in the next two columns, and the per cent of California sales to national sales is given in the last column.

Q. And those on the sheet AZ, what is there shown?

A. That is the California breakdown by months of 1945, which is summarized on the previous sheet.

The Court: I can see that this exhibit has not been inspected by the Chamber of Commerce. Your reference there to Lower California would bring you into great disgrace in this community.

The Witness: I apologize for that.

The Court: Lower California is the peninsula that is below the border. This is Southern California.

Q. (By Mr. Foster): By "Lower California," as you have used it, is meant a part of the State of California, the southern part of it, isn't it?

(Testimony of Louis J. Rozier.)

A. That is correct.

Q. And by "Upper California" you meant the part of the State of California which is the northern part?

A. Yes, sir.

Q. Perhaps the least significant part. Is the next sheet, which is tab BA of Plaintiff's Exhibit 6, for identification, a similar summary for the year 1946?

A. That is right. [227]

Q. And the 1947 summary is tab BB?

A. Yes.

Q. And the 1948 summary is tab BC?

A. That's right.

Q. And the first four months of 1949 is tab BD?

A. Yes.

Q. What is tab BE?

A. BE are the national summaries for the year 1945, broken down into types of Viz-aid fixtures, that is, the 40-watt and the 100-watt, and the later developments. This is set up in a standard form.

Q. And the amounts of the sales in units and sales value are set up there?

A. That's correct.

Q. And tab BF is the same for 1946?

A. Yes, sir.

Q. And BG the same for 1947?

A. Yes, sir.

Q. And tab BH the same for 1948?

A. Yes, sir.

Q. And tab BI is for the first three months of 1949?

A. That's right.

Q. Were these compilations appearing on the sheets marked AY to BI of Plaintiff's Exhibit 6, for



(Testimony of Louis J. Rozier.)

identification, prepared by you or under your [228] direction?

A. They were prepared at my request, under the direction of the office manager, because I have nothing to do with the sales records as such.

Q. What records were employed and did you check these figures against?

A. These were taken——

\* \* \*

Q. (By Mr. Foster): Did you make a check to determine that these records or the summations are at least approximately correct, Mr. Rozier?

A. Yes, sir.

Q. And against what records did you check the figures?

A. I made a spot check of the 1945 figures against the cost of sales sheets I obtained from the office. I made a check of the California figures for 1949 against actual salesmen's commissions' copies.

Q. Did you make any check against these cards, inventory records?

A. I also checked all of the figures against copies of our inventory control cards, which are made up on the basis of fixtures put into manufacture.

Q. Those inventory control cards you refer to are these [229] cards which are tabbed BJ of Plaintiff's Exhibit 6, for identification; is that correct?

A. That is correct.

Q. Then appearing here as tab BK is a statistical bulletin, or, would you state what that is?

A. That is a copy of the National Electrical

(Testimony of Louis J. Rozier.)

Manufacturers Association Monthly Report, submitted to us, and the BK tab covers the introductory sheet or first sheet, indicating the companies participating in this report.

Q. Including the plaintiff corporation?

A. That is correct.

Q. And tab BL?

A. BL is the actual report of sales of fixtures under various classifications.

Q. Including a classification which includes the Viz-aid fixture, Plaintiff's Exhibit 13?

A. That is correct. That is considered a two-lamp shielded fixture.

Q. And so identified upon the tab BL?

A. That is correct.

Q. The tab BL, as I understand you, gives the national sales of all of the companies which are members of this organization and listed upon tab BK?

A. All of the company members who are represented.

The Court: Are those in units rather than in dollars? [230]

The Witness: Those are in units, yes, your Honor.

Q. (By Mr. Foster): This report, tab BL, and similar reports from the same company or association, are they used by you and your company in the usual course of business in comparing your company's sales of the Viz-aid fixture like Plaintiff's

(Testimony of Louis J. Rozier.)

Exhibit 13 with the number of sales of units of the same class nationally by the members reporting?

A. That is correct.

Q. And that such use by you and your company is in the ordinary course of business?

A. That is correct.

Q. Now, appearing upon tab BM of Plaintiff's Exhibit 6, for identification, is what?

A. That is a chart of the Viz-aid sales fluctuations by years, given in units in percentage, of Day-Brite Viz-aid sales nationally, of Day-Brite California sales in units and percentage, and the last column indicates the trend of general fluctuation taken from the report which was just shown, by NEMA.

Q. Now, with respect to California do you find that there is a fluctuation different from the fluctuation in the sales of such devices nationally?

A. Yes.

Q. Explain what the difference is.

A. Do you want me to go through the entire thing ? [231]

Q. In general, to show what it was.

A. It indicates here from 1947 to 1948 Day-Brite's Viz-aid business nationally dropped 4.4 per cent. The California drop was 41.4 per cent.

The national drop, as far as NEMA was able to report, was an increase of 10.7 per cent.

The Court: Does that 10.7 per cent apply to an increase in general business conditions, or just lighting fixtures?

(Testimony of Louis J. Rozier.)

The Witness: Just to lamps reported to NEMA.

Q. (By Mr. Foster): Of just one particular class?

A. Just one particular class of units.

Mr. Foster: The significance of that, we will urge, your Honor, is that while the plaintiff's sales of Day-Brite fixtures fell off only four per cent nationally in 1948 over 1947, it fell off in California 41.4 per cent, which we attribute to the defendant's sales of the infringing fixture, whereas the national sales of all such class of fixtures by all of the large companies combined increased actually 10.7 per cent.

Q. (By Mr. Foster): Would you explain what is shown—or, was this compilation on tab BM on Plaintiff's Exhibit 6, for identification, prepared by you?

A. This compilation was prepared by me from the previous figures shown.

Q. What is shown on tab BN, Mr. Rozier? [232]

A. BN are the same figures resolved into chart form, to be more visual. The units are broken down in the left-hand column at 4,000 per line. The years are shown across the bottom, and we have actually plotted this as against the unit figures, with the exception of the NEMA figure, which you will see as a dotted line. And I have taken the multiple of 10, so that the NEMA figure starts just below the Vizaid figure of 40,000, but that actually indicates 400,000 on the NEMA figure. It just so worked out,



(Testimony of Louis J. Rozier.)

and by using the multiple of 10 I was able to get it in to show the trend.

Q. So this graphically shows that the drop in business, in selling the Viz-aid fixture like Plaintiff's Exhibit 13 in California in 1948 over 1947 was much greater than such a drop in the plaintiff's business nationally, and contrary to the general trend——

A. That is correct.

Q. ——of sales nationally by all of the big manufacturers of such fixtures of such class?

A. That is right. [233]

\* \* \*

Q. What is shown on tab BO of Plaintiff's Exhibit 6, [234] for identification?

A. BO is a reproduction of an Electrical Testing Laboratory report on one of the tests of our Viz-aid fixture. The particular test is of the suspension with the two 40-watt tubes.

Q. Are the reports on tabs BP, BQ, and BR, reports on fixtures of the plaintiff like Exhibit 13 by the same laboratory?

A. That is correct.

Q. All paid for by the plaintiff?

A. That is correct.

Q. And were the reports circulated in establishing sales?

A. They have been reproduced in the form you see them and distributed through our representatives and distributors.

Q. Referring to tabs BT, BU, BV and BW, are they examples of other literature distributed by the

(Testimony of Louis J. Rozier.)

plaintiff to its salesmen for their use and distribution to others with respect to the sales of its products, including the Viz-aid fixture like Plaintiff's Exhibit 13?           A. That is correct.

The Court: BS also is in that category, I take it?

Q. (By Mr. Foster): BS also; that is true, is it not?           A. Yes, sir.

Mr. Foster: Now, the whole book, your Honor, with all [235] of its tabbed material and summaries extending from tab A through tab BW is now offered in evidence as Plaintiff's Exhibit 6.

Mr. Miketta: May the court please, I would like to check that. It was not all marked with these various tabs, and I would like to check that during the recess for a few minutes, before your Honor rules on that.

The Court: We will take a recess at this time for a few minutes, and you may check the exhibit.

Mr. Miketta: Thank you, your Honor.

The Court: Is the Day-Brite Company one of the biggest manufacturers of this type of lighting fixture?

The Witness: As far as we can determine, we are among the ten largest in the NEMA group; as far as we can determine.

The Court: Well, making a very fast comparison of your last sheet, I think it was in the year 1948, out of 438,000 units of the Viz-aid style apparently your records show you sold 93,000?

The Witness: Yes, sir.

The Court: Does that sound about right?

(Testimony of Louis J. Rozier.)

The Witness: That is about right.

The Court: About a little less than one-fourth of the total number of the units sold.

Mr. Foster: That is of that particular class of fixture. [236]

The Court: Yes, of that particular unit.

The Witness: That is about it. The sale was right around 100,000 fixtures, and the NEMA figures given to us were about 400,000.

The Court: Then if you say you are one of the first ten,——

The Witness: So far as we can determine, yes, sir.

The Court: ——is there any organization manufacturing these lighting fixtures that is bigger, that has a larger sales volume than your concern?

The Witness: I don't know the actual figure, but Sylvania is larger than we are.

The Court: You might be one of the first ten, and be No. 1, you know.

The Witness: We don't know that we are No. 1. Those figures are not given among the lighting industry.

Mr. Foster: I might say that I understand, your Honor, that to the members of this organization there is mailed a request for information, which is mailed to a receiving agency, and not to the association itself. The receiving agency learns the sales of each of its members through these reports, but does not report from one member to another. It merely sends a card or notice to the association itself that

(Testimony of Louis J. Rozier.)

the member has reported, but does not say what it has reported. Then they make a composite here of all the figures, [237] substantially, so the members know only what they sold and what the total is that all the members sold, but they cannot tell whether they sold more than anyone else. There isn't any record, from which the witness can answer your Honor's question, and the information regarding sales as to each company reported to the association is precluded because of secrecy.

The Court: Then you have to take it the way I did, take your sales as compared to the others?

The Witness: That is correct.

The Court: And then it would not be a complete answer because this particular organization only embraces in its scope some thirty-five companies, and there would be a large number of smaller companies not belonging to the association?

Mr. Foster: This association is only represented as sixty per cent.

The Witness: As far as they can give us, it is about sixty per cent of the industry. [238]

\* \* \*

Q. (By Mr. Foster): Mr. Rozier, to the best of your knowledge are the salesmen of the plaintiff company paid any greater commission on their sales of the Viz-Aid fixture, Plaintiff's Exhibit 13, than on other fixtures of the plaintiff corporation?

A. No.

Q. And the salesmen receive their entire remuneration from commissions, don't they?



(Testimony of Louis J. Rozier.)

A. That is correct.

Q. Are the architects or wholesalers who buy the Viz-Aid fixture, Plaintiff's Exhibit 13, allowed any greater discounts by the plaintiff company from list on that fixture than they are allowed with respect to other Day-Brite fixtures? A. No.

Q. Is there any inducement of any kind, financial or otherwise, offered by the plaintiff corporation to its salesmen or any of the purchasers to induce the sales of the Viz-Aid patented design fixture like Plaintiff's Exhibit 13 preferentially as regards other lighting fixtures sold by plaintiff company?

A. No.

Q. To the best of your knowledge, have there been any re-orders from the same wholesalers and architects of the Viz-Aid fixture, Plaintiffs Exhibit 13? [239] A. Yes.

Q. Are all of the fixtures, lighting fixtures, of the plaintiff corporation sold by it to wholesalers?

A. Exclusively, yes.

Q. The evidence here before referred to shows that the sales of the Viz-Aid fixture, Plaintiff's Exhibit 13, has greatly increased from the beginning. Has the number of wholesale outlets or buyers of fixtures from the plaintiff corporation increased in that period?

A. Our basic wholesalers have not increased in number, no, sir.

Q. The increase in sales, therefore, of the Viz-Aid fixture, Plaintiff's Exhibit 13, indicates re-orders by the same wholesalers, is that correct?

(Testimony of Louis J. Rozier.)

A. Yes, sir.

Q. Have you collected any illustrations of lighting fixtures of the general type and purpose of the Viz-Aid fixture, Plaintiff's Exhibit 13, as made independently by other manufacturers who have sold them? A. Yes.

Q. Do you have such a collection before you?

A. It is here.

Q. That is Plaintiff's Exhibit for identification what number? A. 9. [240]

The Court: That is in evidence, isn't it, Mr. Figg?

The Clerk: No. 9 is in evidence.

Q. (By Mr. Foster): Plaintiff's Exhibit 9, that is the collection of catalogs which you made?

A. That is correct.

Q. In those catalogs do you find that there are illustrated lighting fixtures of different manufacturers capable of using 48-inch tubes? A. Yes.

Q. Fluorescent tubes? A. Yes.

Q. Of different varying lengths and widths and depths? A. Yes.

Q. Would you briefly refer to a few of those catalogs and point out the different dimensions for the width, length and depth there referred to?

And, if the court please, could we indulge your Honor's patience to utilize for a moment the court's book, because I didn't duplicate all of the catalogs in it for my book or Mr. Miketta's.

A. 49½ inches long, 9 inches wide, and 9 inches deep.

(Testimony of Louis J. Rozier.)

Q. That is which one?

A. No. 7183 Ruby Corporal. [241]

The Court: Under tab A.

The Witness: 9 inches wide,  $6\frac{3}{4}$  inches deep by  $49\frac{1}{2}$  inches long. Ruby No. 8077 Admiral.

This is  $49\frac{1}{2}$  inches long, 15 inches wide, 8 inches deep. Ruby No. 7786, Louveron II.

Here is an 8-inch deep, 15 inches wide,  $49\frac{1}{2}$  inches long. Another Ruby Louveron.

Under tab H we have the Garcy Challenger,  $8\frac{1}{2}$  inches high, 15 inches wide, and there is no depth given on that. Rather, length, pardon me.

The Garcy No. 7780; 52 inches long, 7 inches high,  $10\frac{3}{4}$  inches wide.

Emco——

The Court: Under tab H.

The Witness (Continuing): ——No. 4648,  $49\frac{1}{2}$  inches long, 13 inches wide, 17 inches high.

Another Emco, No. 2048 G, 49 inches long, 10 inches wide, 5 inches high.

Dover Electrical Supply.

The Court: Under Tab H.

The Witness (Continuing): No. LF 154-48, 6 inches high, 11 inches wide,  $49\frac{1}{2}$  inches long.

No. LF 234-48, 11 inches wide, 49 inches long.

Guth, No. M-2855, 8 inches high. There doesn't seem to be any other dimension.  $48\frac{1}{2}$  inches long,  $17\frac{1}{2}$  inches [242] wide by 7 inches high. That 8 inches was incorrect. That was evidently the stem.

Guth No. M-2850,  $50\frac{1}{2}$  inches long, 15 inches wide,  $8\frac{1}{2}$  inches deep.

(Testimony of Louis J. Rozier.)

Guth No. M-1970-W, 48½ inches long, 16 inches wide, 5 inches high.

Guth No. M-2290-W, 15 inches wide, 7½ inches high, 50½ inches long.

Do you think it is necessary to go through any more of these?

Q. (By Mr. Foster): I think that is sufficient, Mr. Rozier.

Mr. Foster: I had ordered Plaintiff's Exhibit 6, for identification, into evidence, before the recess, and you wanted to look up something.

Mr. Miketta: May the court please, I frankly don't see any objection. I have no objection to the introduction of the first two portions of that exhibit, but the figures relating to sales starting with that sheet AY are figures which the witness has not personally compiled. [243]

\* \* \*

Mr. Foster: Mr. Rozier, in addition to the checking you have previously referred to in your testimony, you have checked sales figures against the commission sheets which are customarily kept by the company in the regular course of the business as their copies of the invoices mailed out and bearing on those copies the commission percentage, amount of commission, showing what is due and paid to the salesman, is that correct?

The Witness: Those were the commission copies covering the California sales for 1949, I believe it was, that I did check against the sales figures. I checked those personally.



(Testimony of Louis J. Rozier.)

Mr. Miketta: But not other figures? You didn't check any other figures of invoices?

The Witness: At the other end, that is, the 1945 sales, I have those rough sheets there which are our cost of sales sheets, I checked those against the 1945 sales. The interim periods I did not check, no, sir. They were prepared for me by the office.

Mr. Miketta: I am not pressing this objection; I am voicing the objection. I have it on the record. I will abide by your Honor's ruling. [244]

The Court: You say you are not pressing it but you are voicing it.

Does your company have a set of books in which there are listed the sales for each particular year?

The Witness: Not as such.

The Court: As to styles, such as Plaintiff's Exhibit 13?

The Witness: They have the cost of sales sheets where every sale is entered and our cost checked back against that, but they are lumped as they come through. They have commission copies by territories, but there is no general book that could be presented that would show we had sold so many for each of the periods involved.

The Court: The only way you could obtain that would be by a check made against commissions paid in each particular area?

The Witness: That is correct.

The Court: And then segregate sales concerning a particular unit?

The Witness: Yes.

(Testimony of Louis J. Rozier.)

The Court: That is what you have done?

The Witness: Yes.

The Court: You made a spot check of it?

The Witness: It was actually totaled. I made the spot check. [245]

The Court: I say you had it done and then you made spot checks?

The Witness: Yes.

The Court: Of the results?

The Witness: That is correct.

The Court: In view of the stipulation, counsel, as to damages, I am not going to admit this into evidence as having any bearing upon damages. I will, however, admit it into evidence under the theory that we have been talking about as indicating some probative value on the commercial success.

Mr. Miketta: Very well, your Honor.

The Court: Your objection, therefore, will be overruled in part and sustained in part.

The Clerk: Plaintiff's Exhibit 6 in evidence.

\* \* \*

C\*. Typical engraving invoice.

D\*. Typical engraving invoice.

E\*. Typical typesetter invoice.

F\*. Typical electrotyper invoice.

G\*. Typical electrotyper invoice.

H\*. Typical printing invoice.

I. Bulletin No. 10-B.

J. Bulletin No. 10-B-1.

K. Bulletin No. 10-B-1, reprint.

L. Bulletin No. 10-B-3.

(Testimony of Louis J. Rozier.)

M. Bulletin No. 10-B-5.

N. Form OD 456.

O. Advertising space and production Anfenger.

P\*. Typical Anfenger invoice.

Q\*. Anfenger ad production invoice.

R\*. Ad No. 93.

S\*. Anfenger invoice.

T\*. Anfenger production invoice.

U\*. Ad No. 98.

V\*. Anfenger invoice.

W\*. Anfenger ad production invoice.

X\*. Ad No. 100.

Y\*. Anfenger production invoice.

Z\*. Ad No. 107. [247]

AA. Bloch Advertising Summary, 1946.

AB. Bloch Advertising Summary, 1947.

AC. Bloch Advertising Summary, 1947.

AD. Bloch Advertising Summary, 1948.

AE\*. Bloch ad production invoice.

AF\*. Ad No. 900-A.

AG\*. Bloch ad production invoice.

AH\*. Ad No. 900.

AI\*. Bloch ad production invoice.

AJ\*. Ad No. 911.

AK\*. Bloch ad production invoice.

AL\*. Ad No. 318.

AM\*. Bloch ad production invoice.

AN\*. Ad No. 216.

AO\*. Bloch statement.

AP\*. Ad production invoice.

AQ\*. Ad No. 298.

AR\*. Ad space invoice.

(Testimony of Louis J. Rozier.)

AS. Gardner Advertising Summary, 1949.

AT\*. Gardner production invoice.

AU\*. Ad No. 199.

AV\*. Gardner ad production invoice.

AW\*. Ad No. 249.

AX\*. Gardner ad space invoice.

AY. Viz-Aid Sales Summary, 1945-1949. [248]

AZ. Viz-Aid California Sales, 1945.

BA. Viz-Aid California Sales, 1946.

BB. Viz-Aid California Sales, 1947.

BC. Viz-Aid California Sales, 1948.

BD. Viz-Aid California Sales, 1949.

BE. Viz-Aid National Sales, 1945.

BF. Viz-Aid National Sales, 1946.

BG. Viz-Aid National Sales, 1947.

BH. Viz-Aid National Sales, 1948.

BI. Viz-Aid National Sales, 1949.

BJ. Copies inventory control cards.

BK. NEMA membership list, December, 1948.

BL. NEMA Statistical Bulletin, March 4, 1949.

BM. Viz-Aid Sales Fluctuations.

BN. Graph of Sales Fluctuations.

BO. ETL Report No. 325634.

BP. ETL Report No. 325631.

BQ. ETL Report No. 315756.

BR. ETL Report No. 315757.

BS. ETL Sales Manual, Sheet 2-A-1.

BT. ETL Sales Manual, Sheet 1-A-1.

BU. ETL Sales Manual, Sheet 1-A-2.

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\*Copy for Court only. [249]



(Testimony of Louis J. Rozier.)

BV. ETL Sales Manual, Sheet 1-A-3.

BW. Bulletin, "It Happened in Denver Schools."

\* \* \*

Q. (By Mr. Foster): I wish to direct your attention to the volume which is marked Plaintiff's Exhibit 11, for identification, and to tabs C, D, E, F, of that booklet. These are photographs, C being marked "Ruby Accused Paramount Fixture," D being marked "Plaintiff's Patented Viz-Aid Fixture," E being marked "Ruby Accused Paramount Fixture," and F being marked "Plaintiff's Patented Viz-Aid Fixture."

Two pictures were made of two different positions of each of the devices, your Honor.

Were these photographs made under your supervision and direction? A. Yes, sir.

The Court: Are the photographs which are tabs D and F photographs of Plaintiff's Exhibit 13 here in evidence?

The Witness: That is correct.

Q. (By Mr. Foster): And they accurately portray that exhibit? A. Yes.

Q. And are the photographs which are tabs C and E of Plaintiff's Exhibit 11 for identification photographs of the Ruby device which is Plaintiff's Exhibit 14 or 15? A. It is 14.

Q. Here in evidence?

A. The one that is mounted.

Q. And those photographs correctly depict [250] Plaintiff's Exhibit 14? A. Correct.

(Testimony of Louis J. Rozier.)

Mr. Foster: The photographs identified by the witness, identified as tabs C, D, E, and F, Plaintiff's Exhibit 11 for identification, are offered in evidence as Plaintiff's Exhibits 11-C to -F respectively. [251]

\* \* \*

The Court: Exhibits for identification 11-C, -D, -E and -F are admitted in evidence.

\* \* \*

Mr. Foster: Will you stipulate that G and H of Plaintiff's Exhibit 11, for identification, were distributed by the defendant prior to the filing of the complaint?

\* \* \*

Mr. Miketta: They were printed and probably distributed [252] by the defendant.

Mr. Foster: I will offer the illustrations G and H as Plaintiff's Exhibits 11-G and -H, in evidence.

The Court: Received in evidence.

\* \* \*

Q. (By Mr. Foster): Now, I wish to direct your attention, Mr. Rozier, to tab K of Plaintiff's Exhibit 11, for identification, where there is a title "Some Identities of Patented and Accused Designs."

May the record show that I pass over the first nine items there because those are the nine items I feel which are set forth as identical dimensions within working tolerances in Plaintiff's Exhibit 11-I.

(Testimony of Louis J. Rozier.)

I will ask you if you have checked the remaining items from 10 on and found the identities there identified in Plaintiff's Exhibit 13, that is, the Day-Brite fixture, and Plaintiff's Exhibits 14 and 15, the accused fixtures?           A. I have.

Q. Will you take them up in order and refer to each? The first is No. 10. Is that illustrated, the identity of the entire outline of the end cap, in Plaintiff's Exhibit 11-I? [253]

A. Yes, sir, it is illustrated in the duplicate drawings.

Q. No. 11 is the lower decorative cap panel with its lower edge horizontal. What is indicated there?

A. They are identical as far as appearance is concerned. [254]

\* \* \*

Mr. Foster: I offer it for that limited purpose, tab K of Plaintiff's Exhibit 11, for identification, into evidence.

The Court: It will be admitted into evidence as listing the contentions of the plaintiff of the identities of the patented [255] and the accused designs.

Mr. Foster: A and B are the patents in suit, and I think they were received in evidence. If not, I offer them at this time.

The Court: A and B will be received in evidence. They probably are duplicated in the file wrappers.

\* \* \*

The Clerk: That means, then, that the entire Exhibit 11 is in evidence.

(Testimony of Louis J. Rozier.)

The Court: The entire Exhibit 11 is in evidence with the limitations heretofore placed upon it, except that its title should be modified. It now reads "Exhibits Establishing Infringement and Copying." It should read "Exhibits Contended by the Plaintiff to Establish Infringement and Copying."

Mr. Foster: Very well, your Honor.

The Court: I will add that on the front.

Mr. Foster: That concludes the direct examination, your Honor.

The Court: Likewise, on 11-K, that was admitted for the purpose of showing plaintiff's contentions. The same notation should be made, inserting the words "contended by plaintiff to establish infringement." I will also put in the word "alleged" after the word "some" on the second line. "Alleged [256] identities." Since these are admitted only as contentions. [257]

\* \* \*

#### Cross-Examination

By Mr. Miketta: [258]

\* \* \*

Q. Now, the various tear sheets, so-called, which exemplify the advertising put out by the plaintiff are in two volumes marked Exhibits 7 and 8, are they not?      A. Yes.

Q. Is it not a fact that a great deal of the advertising matter which has been prepared by you and your agencies was directed to the functional and engineering aspects of the fixture?



(Testimony of Louis J. Rozier.)

\* \* \*

The Witness: Part of the—I believe you are speaking [259] here of the “functionally designed” and “optically engineered”?

Q. (By Mr. Miketta): That is right.

A. That is partially the advertising agency’s poetic license, or whatever you may call it.

\* \* \*

Q. (By Mr. Miketta): What is the representation in red, which appears on the tear sheet dated June, 1946, “Electrical Wholesaling”? Do you know?

A. It is a design based on a typical distribution curve.

Q. One of the E.T.L. distribution curves; is that correct?

A. I can’t say whether it is based on an E.T.L. curve. It is just a distribution curve.

Q. A light curve?

A. A light curve; yes, sir.

Q. And that is really directed to engineers, building superintendents, purchasing agents of the State or County, is it not?

A. Hardly, in “Electrical Wholesaling.” [260]

Q. The wholesalers furnish devices, in turn, to these various architects, do they not?

A. The wholesalers do, but this is directed to the electrical wholesalers.

Q. Is that the only time that type of ad has appeared?

(Testimony of Louis J. Rozier.)

A. No, it has run in other publications.

Q. It ran in "Architectural Record" probably, and in various other magazines, did it not?

A. Probably.

Q. Now, do you find anything in that advertisement which uses the words "aesthetic, beauty, ornamentation," or any such words?

The Court: Referring to?

Mr. Miketta: Still referring to this——

The Court: To the June, 1946, "Electrical Wholesaling" tear sheet?

The Witness: I find "Better taste" here, "pleasing designs," "compliment the architectural treatment of any installation requirement."

Q. (By Mr. Miketta): What else?

A. Along that line?

Q. Yes.

A. Nothing else in this particular ad.

Q. All right. Now, I call your attention to an ad appearing in Exhibit 8, apparently from "Electrical [261] Construction and Maintenance" of September, 1947. Is it not true that this ad is particularly directed to emphasis on the snap-on enclosure arrangement, whereby you can drop the entire housing and its connected louvers from the chassis and tubes?      A. That is correct.

Q. Of course, that type of advertising has been placed by you in many publications, has it not?

A. That is correct.

Q. As evidenced by another clipping from the August, 1947, issue of what?

A. That is an engraver's proof. It is not an

(Testimony of Louis J. Rozier.)

actual tear sheet. Sometimes these are engraver's proofs. That was an August, 1947, ad that ran in some of the publications.

Q. Probably in more than one?

A. It probably did, yes, sir.

Q. I call your attention to the ad on the opposite page, also dated August, 1947, which apparently appeared in some publications,—

A. Right.

Q. —is that correct?

A. That is correct.

Q. And that calls attention to what? What is that element?

A. That is the spring clip that supports the enclosure on the chassis. [262]

Q. And permits the removal or the dropping of the chassis in this manner?

A. That is correct.

Q. —which is indicated on the opposite page?

A. That is correct.

Q. That particular function or that particular arrangement, mechanical arrangement, cannot be found in the defendant's structure, can it?

A. No.

Q. Approximately what percentage of your advertising expenditures were directed to those engineering and functional details and structural details, and what percentage of your advertising was directed to the aesthetics and the appearance? Can you make an estimate?

A. I can't even make a rough guess, no, sir.

(Testimony of Louis J. Rozier.)

\* \* \*

Redirect Examination

By Mr. Foster:

Q. Were there any ads of the Viz-Aid fixture, Plaintiff's Exhibit 13, published in magazines, to your knowledge, which didn't contain an illustration showing the appearance of that fixture, and which contained only engineering or [263] technical information about it? Was there any such ad published?

A. You mean, was there any such ad on the Viz-Aid without an illustration of at least one fixture?

Q. Yes. A. No, there never was.

Mr. Foster: That is all.

\* \* \*

The Court: We haven't seen this light on, have we,—the defendant's light?

Mr. Foster: I don't believe we have, your Honor.

(The light referred to was turned on and lighted.)

\* \* \*

Mr. Miketta: While your Honor is observing the fixture, which is the defendant's fixture, I wish to call attention to the fact that the ends are perforated and light shines there through.

The Court: It differs, so far as the perforation is concerned, in that on the plaintiff's device there is some kind of a glass? [264]



Mr. Miketta: There is an opaque member.

The Court: It is opaque throughout, while in the defendant's fixture there is nothing except a space.

Mr. Miketta: Yes, your Honor.

The Court: What are those,—40-watt?

Mr. Foster: 40-watt, yes, sir. [265]

\* \* \*

The Court: You are offering the stipulation and the notice attached thereto?

Mr. Foster: Yes.

The Court: It is in the file. It will be received in evidence as Plaintiff's Exhibit 17. [268]

\* \* \*

### ALBERT JASSIM

called as a witness by and on behalf of the plaintiff, under Rule 43(b) of the Federal Rules of Civil Procedure, having been first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Foster:

Q. Will you state your full name, please?

A. Albert Jassim.

Q. Your residence, please?

A. 730 North Kilkea.

Q. And your age?           A. 36.

Q. You are the same Mr. Jassim who gave your deposition in this action in my office in Los Angeles on May 23, 1949, and you have read the reporter's transcript of that deposition and found

(Testimony of Albert Jassim.)

it all true and signed it under oath, haven't you, Mr. Jassim?      A. Yes. [270]

\* \* \*

The Court: You are calling this witness under 43(b)?

Mr. Foster: Yes, your Honor, under 43(b), and I will lay the foundation for that next.

Q. Mr. Jassim, I understand that you are now secretary of the defendant corporation and have been so since about May, 1947, is that correct?

A. Secretary and assistant treasurer.

Q. And a member of the board of directors?

A. Yes, sir.

Q. And that you have been employed by the defendant corporation since May, 1947, full time in the activities of the company, is that correct?

A. Yes, sir.

The Court: '47?

Mr. Foster: Yes, sir.

Q. And that your work for the company is now and has continuously been, since your first employment by the defendant, in connection with the purchasing and the financial side, keeping of books, and the operation of the office, is that true?

A. Yes. Since then I have been a little more on the outside. [271]

\* \* \*

Q. Since you gave your deposition in the action in May of 1949 you have worked more outside?

A. Yes.

(Testimony of Albert Jassim.)

Q. Has that outside work been selling the lighting fixtures?           A. Yes, sir.

Q. Such as Exhibits 14 and 15, the Paramount lighting fixture of the defendant corporation?

A. Lighting fixtures. I have been selling lighting fixtures, more on the selling end.

\* \* \*

Q. (By Mr. Foster): I direct your attention to a catalog which was marked in your deposition Exhibit 5, for identification, bearing on its cover the title "Lighting by Ruby," [272] and particularly I direct your attention to pages 8 and 9 thereof.

\* \* \*

Q. (By Mr. Foster): The catalog has been re-numbered for these proceedings as Plaintiff's Exhibit No. 18 for identification. I direct your attention to that exhibit and particularly pages 8 and 9 thereof and ask you when you first saw that catalog and those pages.

A. Well, my recollection would be when I first came with the firm.

Q. That is in May, 1947, you first saw that exhibit?           A. Somewhere about that time.

Q. And that catalog was by the defendant corporation mailed out, was it not, to prospective customers to the extent of about 1,000, is that correct?           A. Yes, sir, I would say so. [273]

Q. And that mailing was about May, 1947?

A. Yes, sir, somewheres there.

(Testimony of Albert Jassim.)

Q. And it was mailed to all of the prospective customers then had upon the mailing list of the defendant corporation?

A. Well, not all. There are times when we get new accounts and drop others, but I would say most of the people that we had on our books.

Q. Were any of the fixtures, such as illustrated upon pages 8 and 9 of Plaintiff's Exhibit 18, for identification, sold in May, 1947, by the defendant corporation?

A. They were sold in 1947. I wouldn't quite answer that they were sold in May. But they were sold during the year of 1947.

\* \* \*

Q. (By Mr. Foster): There has been marked a catalog sheet by the clerk as Plaintiff's Exhibit 19 for identification, being the same sheet which was in the deposition Exhibit 4. I direct your attention to the sheet Plaintiff's Exhibit 19, for identification, entitled "The Paramount." Do you recall that you saw that sheet when you went to work for the defendant corporation in May, 1947?

A. I must have seen it, but I am not too well acquainted. [274] My recollection would be that this is the unit that was sold (indicating).

Q. By "this" you mean Exhibit 18, for identification?      A. That's right.

Q. But you do recall that you did see the sheet 19 for identification in the offices of the defendant corporation?



(Testimony of Albert Jassim.)

A. Yes, sir, I must have seen it. I don't quite recollect that.

Q. Were those sheets, 19 for identification, by the defendant corporation mailed out or distributed at any time since you have been with the company?

A. Well, I don't recall any sheets being mailed as single sheets, but I do recollect the catalog being mailed. [275]

\* \* \*

Mr. Foster: The catalog Exhibit 18, I offer the entire catalog as Plaintiff's Exhibit 18.

The Court: It will be received in evidence as Plaintiff's Exhibit 18.

Mr. Foster: And the single sheet marked 19 for identification is offered in evidence as Plaintiff's Exhibit 19.

The Court: It will be received in evidence.

\* \* \*

Q. I show you a catalog marked Plaintiff's Exhibit 20 for identification and call your attention particularly to pages 5 and 6.

The Court: Is this another catalog?

Mr. Foster: Yes, your Honor.

Q. And particularly the two sides on page 5. Do you recall that that catalog containing that page was by the plaintiff corporation distributed in 1949? [276]

A. Yes, sir.

Q. About what month? A. I don't know.

Q. About the middle of the year?

A. Somewhere around there.

(Testimony of Albert Jassim.)

Q. And it was also distributed to about a thousand prospective purchasers of the defendant corporation?

\* \* \*

A. The catalogs were distributed in thousands, but the prospective purchasers are not in the thousands.

Q. And fixtures, Paramount fixtures, of the defendant corporation, as illustrated and identified in Plaintiff's Exhibit 19 and Plaintiff's Exhibit 20, for identification, were sold by the defendant corporation, were they not?

A. Yes, sir, they were.

Q. And when did those sales commence to the best of your knowledge? [277]

A. Well, during the year '47 I would say they commenced.

Q. Probably in May or June of 1947?

A. I would say the year. I wouldn't know just what month we started to sell these fixtures.

Q. And those sales of that fixture continued by the defendant corporation from May or June, 1947, until the present?      A. Yes, sir.

Q. And those sales have been made in Southern California, have they not, and in Los Angeles County?      A. Yes, sir.

Q. And it is a fact, is it not, that up to May of 1949, at least, the far greater percentage of the sales of that fixture were made in California than in the rest of the country?      A. Yes, sir.

Q. And your estimate is that up to at least May

(Testimony of Albert Jassim.)

of 1949 about 90 per cent of the sales of the fixture were made in California by the defendant corporation?      A. Yes, sir, I would say that.

Q. Wouldn't you also say, Mr. Jassim, that through all the period of time during which the defendant has sold this Paramount fixture illustrated in Plaintiff's Exhibits 19 and 20 for identification, 90 per cent of its total sales have [278] been in California?      A. Yes, sir.

Mr. Foster: The catalog marked Plaintiff's Exhibit 20, for identification, is offered into evidence as Plaintiff's Exhibit 20.

The Court: It may be received in evidence. [279]

\* \* \*

Q. (By Mr. Foster): These exhibits, Plaintiff's Exhibits 18, 19 and 20, Mr. Jassim, I note contain not only information as to the size or dimensions of the fixture, but a pictorial representation of it showing the underside, the lateral sides, and the end of the fixture?      A. Yes, sir.

Q. Now, why is it, if you know, that these catalogs of the defendant corporation contain such a pictorial representation of the fixture?

A. Well, that's for the engineers. Everything on that page is—would be pertaining to engineering. In other words, you have to show a picture for a man to see the shape. There is different shapes of fixtures, but then as you get down to the information, there is everything pertaining to the engineering right here (indicating). That is all en-

(Testimony of Albert Jassim.)

gineering data. The shape and the size are all engineering data. That has to be fitted into spaces, and with reference to the ceiling; like curves, efficiency,—that is all pertaining to engineering.

Q. Mr. Jassim, the record doesn't show what you mean when you say "this" and "that." You are pointing to the line drawings which appear upon page 5, and the curves which appear upon page 6 of Plaintiff's Exhibit 20, as indicating the information that must be shown; that is correct, isn't it? [280]

A. That is correct.

Q. Now, my question is directed to the pictorial representation which is at the top of page 5 of Plaintiff's Exhibit 20, which has no dimensions upon it, or angles, or indications of the lighting efficiency. Why is that inserted, if you know, in this catalog, Plaintiff's Exhibit 20? Why isn't there used in the catalog only this engineering information, which you identify?

\* \* \*

The Witness: Well, we start everything with a picture. In other words, we start everything with a certain form. A man has to know whatever to show a man. He has to know what it looks like basically. Then we go along and give the man—in other words, we do everything. We sell fixtures to the wholesale jobbers, but we promote our fixtures through the engineers and architects.

Naturally, he has to see what the fixture looks like, to have an idea, but from there, of course, you



(Testimony of Albert Jassim.)

go right to the engineering data. In other words, it is unusual for him not to refer to the fixture with the engineering data. He has to have that, and he has to have an idea also what the fixture looks like. You can't just sell him engineering data, without an idea what the fixture itself looks like. [281]

Q. (By Mr. Foster): Well, as I understand your testimony, then, these catalogs, Exhibits 18, 19 and 20, contain a pictorial illustration of the Paramount lighting fixture because the company has found it is necessary for the purchasers to see what the fixture looks like, its over-all appearance, before they buy it, as well as to know the dimensions and the technical information about it; that is a fair statement? A. Yes, sir; that's right.

Q. And I judge from that that you and the defendant have found it is necessary, in order to induce others to purchase the fixtures of the defendant, that the purchaser should conclude that the fixture has a desirable, pleasing appearance, as well as meeting technical qualifications; that is a fair statement, isn't it? A. Yes.

Q. I notice throughout all of this catalog, Exhibit 20, that there are a number of illustrations of other fixtures, lighting fixtures, using fluorescent tubes, from which I think it is a fair conclusion that the defendant corporation has found it necessary to let prospective purchasers see the different fixtures of its manufacture not only have pleasing appearances, appealing to the eye, but they have different appearances so that the purchasers can

(Testimony of Albert Jassim.)

select those fixtures having a pleasing appearance that is [282] particularly appealing to them; is that a fair statement?

A. Well, I will say it. Basically, we manufacture a fixture from the study of light. We approach a fixture from the amount of efficiency of light, or spread, or upper or down light that we get out of it. It assumes shape as our engineering division shows us that it will do so-and-so, and so-and-so. Now, when it gets to that part of it, you sort of hold yourself down to certain dimensions, to get a certain amount of light out of it. Then it starts to take shape. Naturally, you could say if it is not pleasing it is not merchantable, and you certainly have to have it pleasing.

Q. In order to sell a lamp?

A. Well, sure. It has to have the efficiency of light. That's the basic point. That's the important point.

Q. I note in looking through this Plaintiff's Exhibit 20 that some of the fluorescent light tube fixtures, for example, back of page 2, have a length of  $48\frac{1}{8}$  inches, and some of them, for example, a picture on the back of page 6, has the length of  $49\frac{1}{2}$  inches, and some of them have a width of 14 inches, that is the back of page 6, and some of them have a height of 7 inches, the same page, whereas the Paramount fixture on the back of page 5 has a height of  $61\frac{1}{4}$  inches, and a width of  $12\frac{3}{4}$  inches. Those height and width dimensions are chosen in accordance with the selection of a design which is

(Testimony of Albert Jassim.)

sought to be appealing to the [283] eye; is that correct?

A. No. We select fixtures for the efficiency of light. In other words, we can't make the same type of fixture for every room, so we engineer fixtures to—in other words, if you go in a super-market you make one type of fixture, because you want a certain spread of light in the super-market. If you go to an office, you make another type fixture to give it a different type of efficiency. And these fixtures assume different shapes for the reasons of the different type of installations that you make. [284]

\* \* \*

Q. Directing your attention to page 5, the fixture there, that is made in a form where it has only two light tubes, hasn't it? A. Yes, sir.

Q. On the same level horizontally? Side by side, they are horizontally on the same level?

A. Yes, sir.

Q. I notice it has a width of  $12\frac{3}{4}$  inches and a height of  $6\frac{1}{4}$  inches, as compared with this other one you have referred to, which has a height of 5 inches and a width of  $12\frac{1}{2}$  inches. Where is that fixture on page 5 used?

A. This fixture here (indicating)?

Q. Yes.

A. Well, it would be used in drafting rooms, in certain offices.

Q. Well, do you recall any lamp fixture which is sold by the defendant corporation and advertised

(Testimony of Albert Jassim.)

in any catalog sheets distributed by the defendant corporation, which catalog [285] sheets do not contain a pictorial representation showing the appearance of that lighting fixture?

A. Well, I don't know of any advertising that doesn't show any pictorial. There are some. I have seen some, but mostly they would show that.

Q. Almost without exception all literature distributed by the defendant corporation with respect to its lighting fixture contains a large pictorial representation, so that the reader can see what the lighting fixture looks like, in order for him to determine whether it is appealing to his eye; that is true, isn't it?

A. Yes, sir; it is. [286]

\* \* \*

Q. Is it your opinion that the Paramount fixture illustrated in Plaintiff's Exhibits 18, 19 and 20 differs in its over-all appearance from the other fixtures shown in the defendant's catalogs, Exhibits 19 and 20?

A. Well, all fixtures are different.

\* \* \*

Q. Is it your opinion that the over-all appearance of the Paramount fixture illustrated in the Exhibits 18, 19 and 20 differs from the over-all appearance of the other fixtures of Defendant's manufacture illustrated in those catalogs?

A. Yes, sir, it does.

Q. Now, having regard to the over-all appearance of the Paramount fixture, which is in evidence



(Testimony of Albert Jassim.)

here as Plaintiff's Exhibits 14 and 15, what is there to your mind that distinguishes that appearance from the over-all appearance of the other fixtures of the defendant's manufacture, and will you state that, without studying any of the fixtures that are here in court, looking at the judge or myself?

A. Well, I would say the shape was a little different. It has a little different type of baffle on it.

Q. Do I understand that the over-all outline, for example of a section across the fixture, and the arrangement of the transverse and longitudinal louvers, to your mind, contribute to the over-all appearance of the Paramount fixture, which distinguishes it from the over-all appearance of the other fixtures of the defendant's manufacture; is that a fair statement?

A. The full shape is different than the other fixtures. If you refer to any particular feature itself, there are fixtures in our line that have the same features as the Paramount. [290]

Q. But to your mind, as I understand your previous answer, it is the shape, for example, of the ends of the fixture and the arrangement of the longitudinal and transverse baffles that enables you to distinguish the over-all appearance best of the Paramount fixture from the others of defendant, that is true, isn't it?

A. I wouldn't answer that. I would answer it in the respect that it has a little bit different shape than the other fixtures. But when you talk about

(Testimony of Albert Jassim.)

the louver, we apply that same idea to other fixtures.

Q. What did you mean when you said one of the two things to your mind that made the Paramount fixture appearance distinctive was the louvers?      A. The shape of it.

Q. The shape of the louvers?

A. The shape of the fixture itself.

Q. You mentioned louvers. What is there about the louvers of the Paramount fixture that make it distinctive from other fluorescent lighting tube fixtures?

A. We have different types of louvers with different spacings.

Q. That is the spacing and the number of the louvers, transverse louvers, and the shape of the longitudinal louver, that is what you meant?

A. Yes. [291]

Q. What is there other than those features of the louvers that make the appearance of the Paramount fixture distinctive in your opinion from all other fixtures of the defendant, the over-all shape you have mentioned? Is there anything else?

A. It is very hard to answer that because there are a lot of fixtures that are very similar to the Paramount fixture.

\* \* \*

Q. Haven't we agreed, Mr. Jassim, that in your opinion the appearance of the Paramount fixture of defendant is distinctive from the over-all ap-

(Testimony of Albert Jassim.)

pearance of all other fixtures of defendant? We agree to that, don't we?

A. I made a mistake if I said that.

Q. Don't you think so?

A. There are some features that it isn't too distinctive from. [292]

\* \* \*

Q. Plaintiff's Exhibit 13 is the Viz-Aid fixture of the plaintiff corporation. You have seen that in court here while you have been in attendance, haven't you? A. Yes, sir.

Q. And you saw a Viz-Aid fixture like that prior to the time that you went to work for the defendant corporation, didn't you?

A. I don't think so. I don't really know. [295]

\* \* \*

Q. Did you have anything to do, Mr. Jassim, with the design of the defendant's lighting fixture, Plaintiff's Exhibit 14 or 15, the Paramount fixture?

A. No, sir, I don't think I did. I don't think I was with the firm then. [296]

\* \* \*

Q. But as regards the over-all general appearance to [298] your eye, at least, there is no difference in the appearance of the fixture illustrated in the sheet, which is Plaintiff's Exhibit 19, and page 5 of Plaintiff's Exhibit 20, when I place them side by side in front of you, that is true, isn't it?

A. Just at a fast glance, I would say so.

\* \* \*

(Testimony of Albert Jassim.)

Cross-Examination

By Mr. Miketta:

Q. While you have Exhibit 20 before you, I want to call your attention to the fixture illustrated on page 3 of Exhibit 20. Is it correct that the width of that is  $10\frac{3}{4}$  inches and the over-all height is  $6\frac{3}{4}$  inches?

A. Yes, sir, according to the catalog.

Q. And that also has inclined sides and a step-down end and a louvered bottom, is that correct?

A. Yes, sir.

Q. And the ends are perforated with a certain design, [299] which is illustrated both in the perspective view at the top and also in the diagrams appearing in the center of the page, is that correct?

A. Yes, sir.

Q. And speaking of dimensions, turn to page 11, please. Now, the over-all height of that fixture is 5 inches and the width is  $12\frac{1}{2}$  inches, is that correct? A. Yes.

Q. And I believe you had some difficulty in answering Mr. Foster's question as to whether that was used in a market or not. Will you read what appears in the upper left-hand portion of that page?

A. "The rich looking unit for banks, stores, civic buildings with high ceilings."

Q. In other words, as you glance through this catalog you find that there are various fixtures which are illustrated there, and they range in width



(Testimony of Albert Jassim.)

from approximately  $10\frac{3}{4}$  inches to perhaps 15 or 18 inches, is that correct?      A. Yes, sir, it is.

Q. And they vary in height of the total fixture from 5 inches as in the case of the fixture on page 11 to perhaps 7 or 8 inches, I believe 8 inches was the maximum commented upon, is that correct?

A. Yes, sir.

Q. Now, I call your attention specifically to Exhibit [300] 19, which is that single sheet. Look at that closely instead of casually and tell me whether that particular fixture as illustrated on sheet 19 was ever sold by Ruby Lighting, to your knowledge.

A. No, sir, it never has been.

Q. Why do you say that?

A. I don't ever recollect the design of this center part ever being sold, and I can't understand how it ever got in the catalog, frankly.

Q. In other words, in Exhibit 18 the fixture shown on page 8 differs from that shown on Exhibit 19 in the formation of that medallion or part on the side rails, is that correct?      A. Yes, sir.

Q. But with that exception the rest of the unit is exactly the same, is that correct?

A. Yes, sir, it is.

Q. How are the louvers removed when you want to put the new lamps in?

A. You slide them out of the end, there is an opening in the end, and you slide it right out and it hinges off the other side.

Q. Can you point to a diagram that illustrates that?      A. Yes, sir. Right here (indicating).

(Testimony of Albert Jassim.)

The Court: Referring to Plaintiff's Exhibit 19.

Q. (By Mr. Miketta): In other words, the entire louver assembly—you wouldn't call that sliding, it hinges, doesn't it?

A. Hinges, that's right.

Q. If you will refer to Exhibit 20 and look at page 3, do the louvers in that particular fixture hinge downwardly, too? A. Yes, sir.

Q. And the fixture illustrated on page 5, which is the accused structure, does that again show the louvers hinging down? A. Yes, sir.

Q. When those louvers are hinged down, you don't move the end plates down?

A. No, sir. The end place is stationary. [302]

\* \* \*

### Redirect Examination

By Mr. Foster:

Q. The catalog, Plaintiff's Exhibit 20, was by the defendant sent out or distributed to a certain mailing list or group of people, and the catalog containing the sheet Plaintiff's Exhibit 19 was likewise distributed and sent out to the same group of people, wasn't it?

A. Yes, sir, I would say so.

The Court: Now, just a minute. Has there been any testimony that Plaintiff's 19 was ever in a catalog?

Mr. Foster: I understood that it was.

Is that correct, Mr. Jassim?

(Testimony of Albert Jassim.)

The Witness: I think I made the statement that I have never seen it in a catalog.

Q. (By Mr. Foster): But you do recall that the sheet, Plaintiff's Exhibit 19, was distributed by the defendant corporation?

A. I assume I saw it. I don't remember that I did see it, but I will assume that. Being in the business, I know we made the sheet, so I assume that I saw it. [303]

\* \* \*

Q. That was Plaintiff's Exhibit 4, for identification, as you will see here in the deposition on page 16, and here is the marking "Plaintiff's Exhibit 4, for identification," from the deposition, it is the same sheet as Plaintiff's Exhibit 19; isn't it your recollection of the testimony now that some of this sheet, Plaintiff's Exhibit 19, were distributed by the defendant corporation?

A. Well, maybe I didn't notice the design effect; but as far as I know, as long as the design has been called to my attention, I would say the only one that I recollect is the one that is in the catalog. [305]

\* \* \*

Q. (By Mr. Foster): Did the defendant corporation ever notify the trade that a change had been made in the design of the fixture, Plaintiff's Exhibit 19, as regards the panels in the center of the sides and as compared with Plaintiff's Exhibits 18 and 20?

A. My first recollection of the fixture is just

(Testimony of Albert Jassim.)

exactly the way it is in the catalog. I didn't have anything to do with that sheet, and I may have seen it in our office. But the only recollection I have of the catalog being sent to any of our customers is the way it appears in the catalog as a total.

The Court: Do you know or do you not know whether or not any notice was sent out to the trade or your customers in which any specific reference was made to that sheet which is [308] Plaintiff's Exhibit 19?

The Witness: No, sir, I don't.

\* \* \*

### BENJAMIN RUBY

called as a witness by and on behalf of the plaintiff, under Rule 43(b) of the Federal Rules of Civil Procedure, having been first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Foster:

Q. Is your name Mr. Ruby or Rubinstein?

A. Ruby.

Q. Your full name?

A. Benjamin Ruby.

Q. You are a resident of Los Angeles County and you are president of the defendant corporation, is that correct?

A. That is correct.

Q. Do you recall that you gave your testimony by deposition in this action in my office on the 24th



(Testimony of Benjamin Ruby.)

of May, 1949, and read and signed your deposition there taken? [309]      A. That is right.

Q. And you own some 79 or 80 per cent of the stock of the defendant corporation and have continuously since it was formed, have you not?

A. Correct.

Q. When did you first become associated with the defendant corporation, Mr. Ruby?

A. With the Ruby Lighting Corporation?

Q. Yes.      A. Since the beginning of it.

Q. And that was when?

A. Shall we go back East or in California?

Q. Just this present company.

A. The present company I think was about 1940.

Q. And the Ruby Lamp Manufacturing Company, that was a predecessor, wasn't it?

A. That's right.

Q. With which you were associated in the East?

A. That's right.

Q. And it also dealt in lighting fixtures?

A. Correct.

Q. And after that and before association with the defendant corporation, you were an officer of Ruby Lighting Company, Inc., that is true, isn't it?

A. Correct. [310]

Q. And it also dealt in lighting fixtures?

A. That is right.

Q. And it was adjudged a bankrupt in 1942 and the present defendant corporation took over its assets, is that correct?      A. That is correct.

(Testimony of Benjamin Ruby.)

Q. You have been continuously in attendance here in court during this trial, have you not?

\* \* \*

A. I said I was absent one morning.

Q. Plaintiff's Exhibit 19 is one sheet of a catalog entitled "The Paramount." Was that sheet contained in a catalog distributed by the defendant corporation?

A. Just the sheets were distributed.

Q. And it was distributed to about a thousand people, was it not?      A. Approximately.

Q. That was in 1947?      A. About that.

Q. In approximately what month?

A. The early part of '47.

Q. Who made the design of the fixture which is shown [311] in Plaintiff's Exhibit 19? You made it, did you not?

A. I am not a designer, but it was made under my instructions.

Q. Well, weren't you and you alone responsible for the design of the fixture shown in Plaintiff's Exhibit 19?      A. That is correct. [312]

Q. And helping you in that work was an employee of the defendant corporation known as Bob, was there?      A. That's right.

Q. He was the only one who helped you, and he helped you by making sketches that you told him to make?      A. That's right.

Q. And you don't know the last name of Bob, or where he is?

(Testimony of Benjamin Ruby.)

A. I don't know where he is now.

Q. And you don't know his last name?

A. I can look it up, if it is necessary.

Q. But you don't know it now?

A. I don't remember it. It is a hard name to remember.

Q. And the making of that design——

A. Yes.

Q. ——shown in Plaintiff's Exhibit 19, with the help of Bob, consumed somewhere between a total of 8 to 12 hours, did it not?

A. I don't know the hours because we made about, oh, I would say approximately 8 or 10 different designs.

Q. Just rough sketches which you threw away?

A. That's right.

Q. Isn't it your best estimate it was a few hours and probably less than 10 or 12 that were consumed in reaching the design shown in that exhibit, Plaintiff's Exhibit 19? [313]

A. Yes; a rough design, yes.

Q. And it was your purpose in making that design to provide a general over-all appearance and eye appeal for a fluorescent tube fixture that was distinctly different from the fixtures and their appearance as those fixtures were made by competitors; is that correct?

A. Well, no. The trend of business has been going towards engineered lighting for some time, see, and we had to revamp our line, and we have made about 8 or 10 designs on which 2 or 3 were left to

(Testimony of Benjamin Ruby.)

market, that we did put on the market at the same time, including this one.

Q. But when did you make this design on Plaintiff's Exhibit 19?

A. I would say late 1946 or '47.

Q. When you made that design, the defendant corporation didn't even have an engineer in its employ, did it, Mr. Ruby?

A. No. But our salesmen would come in and say they have got to have engineered lighting, and that's when we started to develop this line.

Q. Are you responsible for the engineering involved in this design, shown in Plaintiff's Exhibit 19?

A. No, sir.

Q. Well, you said there was no one other than Bob who helped you in the design? [314]

A. Yes, sir.

Q. And the company had no engineers in its employ?

A. No.

Q. Was any engineering done upon this design of the Paramount fixture, Plaintiff's Exhibit 19,—

A. No.

Q. —before this?

A. We have tried to make the fixture and placed the lamp in certain positions, and we put a light meter under it, to see what directions, and so forth, by ourselves. We didn't call it engineering, but it was close to it.

Q. You did that before this particular Plaintiff's Exhibit 19 was distributed by the defendant?

A. That's right.



(Testimony of Benjamin Ruby.)

Q. And you did that testing with the light meter in 1947?

A. Yes. We used light meters as far back as '40.

Q. But you used a light meter on the particular fixture, Plaintiff's Exhibit 19,—

A. That's right.

Q. —in 1947? A. That's right.

Q. Before you distributed this sheet?

A. That's right.

Q. No other engineering was done upon this fixture,— [315] A. No.

Q. —shown in Plaintiff's Exhibit 19?

A. No, sir.

Q. And no fixtures precisely like that shown in Plaintiff's Exhibit 19 were ever sold by the defendant, that is, fixtures having a side panel as indicated by the pencil numeral 1 on its side in Plaintiff's Exhibit 19? A. I didn't get that.

Q. Did the defendant corporation ever make a light fixture like that shown in Plaintiff's Exhibit 19 and sell it?

A. Exactly designed like that?

Q. Yes. A. This exact one?

Q. Yes. A. No, sir.

Q. The defendant did make and sell a fixture in all respects like that shown in Plaintiff's Exhibit 19, except it was a slightly different form, as to the ornament in the middle of the side of the fixture, as indicated by the pencil numeral 1 on Plaintiff's Exhibit 19; that is correct, isn't it?

A. We made another fixture, yes.

(Testimony of Benjamin Ruby.)

Q. And it was identical, with that exception?

A. That's right. [316]

\* \* \*

Q. (By Mr. Foster): The fixture identical except for that panel in the side is the fixture that is shown in Plaintiff's Exhibits 18 and 20, and that is what you were referring to?

A. That's correct.

Q. Referring to Plaintiff's Exhibit 19, this decoration, two rectangles in the middle of the side indicated by the numeral 1, was your thought, as well as all the rest of the design; that's true, isn't it?

A. Well, it just come out that way. While you are designing, you try to put in something, and when you go to manufacture, you change your design completely because you can find labor-saving. You see, I also supervise in the factory, and we have this——

Q. But the idea of having that decoration indicated by the numeral 1 on Plaintiff's Exhibit 19 was yours?

A. That's right.

Q. Had you, prior to the time you completed the design shown in Plaintiff's Exhibit 19, seen fixtures of the Day-Brite Company like Plaintiff's Exhibit 13 here in evidence?

A. Well, here, prior to——

Q. Yes, had you seen that light fixture before the time you completed the design shown in Plaintiff's Exhibit 19? [317]

(Testimony of Benjamin Ruby.)

A. I have seen lots of fixtures, but I didn't take particular notice of that. I would go into a place and see 50 or 100 fixtures hanging there.

Q. You don't deny, do you, that you did see the plaintiff's fixture, Plaintiff's Exhibit 13, before you completed the design of the fixture, Plaintiff's Exhibit 19?

A. I don't deny it, and I don't admit it, because I have seen lots of them.

Q. Now, did any other employee of the defendant, or anyone else, help you in completing the design of Plaintiff's Exhibit 19, except this man Bob?

A. Complete it in the design?

Q. In the design, yes.

A. Not that I can remember.

Q. What were Bob's duties there with the defendant corporation? Was he an artist?

A. I would call him a designer or draftsman.

Q. He was a draftsman, was he? A Yes.

Q. Did the defendant corporation receive any orders for lighting fixtures as a result of distributing its leaflet which is Plaintiff's Exhibit 19?

A. Which one?

Q. Plaintiff's Exhibit 19.

A. Is this 19 (indicating)? [318]

The Court: That is 19, yes.

The Witness: I don't recollect if we received orders, but we never made this fixture.

Q. (By Mr. Foster): Did you ever notify any of those to whom you distributed the leaflet, Plain-

(Testimony of Benjamin Ruby.)

tiff's Exhibit 19, that the defendant would not make and sell a fixture exactly as there illustrated?

A. No, we never did, but with a lot of our fixtures, we can just change a little gimmick on it and just ship it without notification.

Q. Because it is so nearly like it?

A. It just doesn't make any difference.

Q. The changes make so little difference in the over-all appearance that it isn't necessary to notify the recipient of the catalog or sheet?

A. It doesn't make any difference in the design.

Q. So that you felt here the appearance of the fixture in Plaintiff's Exhibit 19 and the appearance in Plaintiff's Exhibits 18 and 20 were so nearly alike, that the change in the panel numeral 1 in Plaintiff's Exhibit 19 was so insignificant that it wasn't necessary to notify the purchasers that you were changing it?

A. We didn't notify them.

Q. Is that right?            A. That's right. [319]

The Court: In addition to Plaintiff's Exhibit 19 in evidence, that is that one sheet you have been looking at,—

The Witness: Yes.

The Court: —did this employee Bob, or you and Bob in conjunction, also prepare a blueprint or a specification of this fixture?

The Witness: No, we roughed it out, see.

The Court: Now, what did you rough out? Did you rough out the fixture shown on Exhibit 19 on a blueprint?



(Testimony of Benjamin Ruby.)

The Witness: No, we roughed this out on regular drawing paper.

The Court: Just as you have it there?

The Witness: Yes, on white drawing paper.

The Court: What I am asking you is: what you roughed out on white drawing paper was the fixture shown on Exhibit 19?

The Witness: That's right.

The Court: Or was it a plan with dimensions of the fixture?

The Witness: No, it was with dimensions, like a working drawing for the factory.

The Court: You made a working drawing?

The Witness: That's right.

The Court: In addition to Exhibit 19?

The Witness: That's right. [320]

The Court: And the working drawing had dimensions on it?

The Witness: Yes, sir.

The Court: The height, width, length?

The Witness: Yes, sir.

The Court: Do you still have that drawing?

The Witness: I don't think so. I have been looking through all the drawings, and this man hasn't been with us for some time, and I just couldn't find it.

The Court: You say you never made any of the fixtures shown on Exhibit 19?

The Witness: No.

The Court: But you made the fixtures called "Paramount" shown in Exhibit 18?

(Testimony of Benjamin Ruby.)

The Witness: That's right.

The Court: On pages 8 and 9?

The Witness: That's correct.

The Court: Did you have a blueprint, a working drawing for those?

The Witness: Well, this is after three years. It is very hard to clean the room out, and you change employees.

The Court: Aren't you still making the Paramount design shown on pages 8 and 9 of Exhibit 18?

The Witness: We still make—we haven't made that, I would say, for four, five or six months. [321]

The Court: You made some as late as six months ago, then?

The Witness: Yes.

The Court: Did you have a blueprint or design?

The Witness: No, we have the patterns in the factory, see. We have a pattern like when you cut dresses, or anything else.

The Court: Jigs and patterns and what-not?

The Witness: Yes.

The Court: Do you still have the jigs and patterns?

The Witness: I think we should have it. It becomes a stock body. We use three or four different numbers on the same chassis, as you call it, on the body in there.

\* \* \*

Q. (By Mr. Foster): Let me see if I understand you correctly, Mr. Ruby: After you had completed the design of the fixtures shown in Plaintiff's Ex-

(Testimony of Benjamin Ruby.)

hibit 19, one of them was made by hand by the defendant corporation?

A. That's correct. [322]

Q. Then you looked it over, and approved it, and had the commercial devices made like it, except that this panel indicated by the number 1 was changed?

A. I found labor-saving devices, and we had to change these while we made it.

Q. The labor-saving device has reference to this panel No. 1 on Plaintiff's Exhibit 19?

A. That's correct.

Q. How soon after you had completed the design of Plaintiff's Exhibit 19 did you have this one made in the shop? Was that right afterwards?

A. Oh, I would say several weeks.

Q. Then, as soon as the one was made in the shop,—about when was that made? In '47?

A. In '47.

Q. About May or——

A. The early part of '47.

Q. How soon after was it, after the first one was made in the shop in early '47, that the commercial forms were made and sold? Was it just a matter of a couple of weeks?

A. That's correct. We made dies.

Q. Would you say two or three weeks?

A. After the first one?

Q. Yes. A. A few weeks, yes. [323]

Q. Two or three weeks after the first one was made, your shop started turning out the commercial

(Testimony of Benjamin Ruby.)

product like Plaintiff's Exhibit 19, except for the panel there?      A. That's right.

Q. And what were the steps you took in having this first device made? You just took the sketches that Bob made for you under your direction, showing this design on Plaintiff's Exhibit 19, to your shop and said, "Make one like this"?

A. That's right.

Q. And you told them what dimensions to use in making that one? It was a full-size fixture, wasn't it?

A. It was a full-sized drawing that goes according to dimensions and all. We made ours for the lamps, and we can't go over that, because then the lamps won't go in.

Q. But you selected the dimensions and told the shop?

A. The approximate dimensions that will fit into it.

Q. And those dimensions of the first one, made by the shop under your direction, were the same as the ones that were subsequently made commercially, except for this middle panel, No. 1, on Plaintiff's Exhibit 19?      A. That's correct.

Q. But all that they had in the shop to make that first fixture, Paramount fixture, like Plaintiff's Exhibits 18 and 20, were these sketches that Bob made for you,— [324]

A. That's correct.

Q. —and the dimensions you gave them?



(Testimony of Benjamin Ruby.)

A. That's correct.

Q. Then when the fixture was produced commercially, like Plaintiff's Exhibits 18 and 20, all your shop had to go by was the fixture that was first made, incorporating your design that you have just referred to?

A. That's correct.

The Court: He told me that they made a blueprint to work from.

The Witness: A working drawing on a white paper.

The Court: A working drawing on a white paper.

The Witness: Yes, sir.

The Court: Rather than a sketch.

The Witness: That's right.

Q. (By Mr. Foster): When the first one was made incorporating this design, was there a drawing on white paper with all the dimensions?

A. Yes, a working drawing.

Q. Even before the first fixture was made?

A. Yes.

Q. Then the same working drawing with all dimensions was used in the shop to produce the commercial fixture like Plaintiff's Exhibits 18 and 20?

A. Yes, with a few minor changes, where you could save [325] on the labor, or something.

Q. And Bob worked out that drawing?

A. Yes, sir.

Q. And you gave him the dimensions to put on it?

A. That's correct.

Q. And that included the number of louvers, and the height and width of the fixture, and so on?

(Testimony of Benjamin Ruby.)

A. That's correct.

Q. Now, what made you select the values you did for the height and the width of that fixture? How did you get those dimensions?

A. Well, we go by the—by all lighting fixtures. They are all about the same height or width, within fractions different.

Q. Did you take the height and width and length dimensions involved in Plaintiff's fixtures 14 and 15 off of some other fixture?

The Court: Just a minute. You mean Plaintiff's Exhibits 14 and 15?

Mr. Foster: Yes, Plaintiff's Exhibits 14 and 15. I am sorry, your Honor.

The Witness: No, on all lighting fixtures we studied the height so as to have room enough for ballast and room enough for the lamps and room for a louver to swing. In 99 out of a hundred fixtures they are about the same height. [326] You have to have that amount of height to have the lamps and the ballast.

Q. (By Mr. Foster): How did you get the height of the fixtures, Plaintiff's Exhibits 14 and 15?

A. Just by drawing it up.

Q. And the length the same way?

A. Yes.

Q. How did you happen to fix on the No. 13 as the number of transverse louvers, instead of 10 or 18, or some other number?

A. Well, if you have them too wide apart, you would see the lamp, and if you close them too much,

(Testimony of Benjamin Ruby.)

you don't get the light through. You go according to what the fixture will demand for the light output and still be shielded.

Q. This drawing that was made before the first device was made there in your shop, that drawing had 13 transverse louvers in it, didn't it?

A. I think we had 15 in it.

Q. Then you changed it, after the first one was made, to 13, did you?

A. No, we never changed it.

Q. How many transverse louvers does the defendant's fixture have, Plaintiff's Exhibits 14 and 15?

A. 15. One at each end, and 13 through. The whole louvers consist of 15. [327]

Q. And the first drawing made by Bob for you with this design, before any fixture was made, had the same number of transverse louvers in it as the commercial form which is Exhibits 14 and 15?

A. That's correct.

Q. That drawing had that number of louvers because you told Bob to put them in there?

A. Not that I told him. When you have the same people, you figure just about what you must have.

Q. He didn't determine the number? You determined that, didn't you?

A. Well, we determined it by the amount that there must be on there. We may have started with less or more, but it won't lay out in the plans, see. You keep going until you know it is right.

(Testimony of Benjamin Ruby.)

Q. You say you were the one that was entirely responsible for this design. Did you select the number of transverse; louvers that are in your fixtures, Plaintiff's Exhibits 14 and 15?

A. Well, I could say yes.

Q. Did you try it out with any different number of transverse louvers?

A. No. When you put it on the paper, see, you can see right then and there you can't have six and you can't have sixteen. [328]

Q. You put 15 in there the first time, and you were satisfied, and you let the number remain?

A. That's right.

Q. And you chose 15 because you thought that was a good number?

A. No. When we put it up, we put it up to distribute the light good, because the distribution must be accurate.

Q. But you say on this drawing, which was made before any fixture was made, you put on 15 transverse louvers? You chose that number?

A. No. As we go along, we make the fixture and see how many. First we make the body, and the end casting, and we work it right into it.

Q. Now, the drawing you just made on white paper?

A. Yes.

Q. And as I understood you, the drawing was made before any fixture was made at all?

A. Yes.

Q. And that had 15 transverse louvers on it?

A. It may have had 15.



(Testimony of Benjamin Ruby.)

Q. It had that because you selected that number rather than any different number? A. Yes.

Q. And your answer is that you just guessed 15 would be a good number rather than any other number; is that right? [329]

A. Yes, it would lay it out in a good proportion.

Q. You didn't try out on paper, or any other way, any different number of transverse louvers, did you? A. No.

Q. Now, no one has applied, no one connected with the defendant have any design patents upon this Paramount fixture, Plaintiff's Exhibits 14 and 15, have they? A. No, sir.

Q. And you haven't applied or caused to be applied for design patents on the fixture, because you believe that the design patents would not prevent anyone from making the same fixture; that is true, isn't it?

A. Yes, sir; from experience. I can explain why.

Q. You did not apply or have anyone apply for the design patents on the fixture, Plaintiff's Exhibits 14 and 15, because from your experience you believed anyone could make a little change in the design and get around the patent; that is right, isn't it? A. It has been done to me.

Q. Well, that is the reason you didn't apply; isn't that right. A. Yes.

\* \* \*

Q. By Mr. Foster: You remember that you did receive [330] this notice of infringement, dated

(Testimony of Benjamin Ruby.)

August 12, 1947, on behalf of the plaintiff, which is Plaintiff's Exhibit 17, didn't you?

A. Yes, sir.

Q. Did you take any steps to diminish your sales or attempts to sell the Paramount fixture, Plaintiff's Exhibits 14 or 15, because of that notice of infringement?

\* \* \*

The Witness: I took no steps at all. I couldn't recall my catalogs, or anything, and did nothing about it.

Q. (By Mr. Foster): Well, you continued with the same degree of effort to attempt to sell this Paramount fixture, Plaintiff's Exhibits 14 and 15, after you got the notice of infringement, as you did before, didn't you? A. Yes, sir.

Q. I direct your attention to Plaintiff's Exhibit 10, entitled "Prior Art Designs from Patents," and direct your attention to tabs numbered or letters B, and C, and AH. Would you look at B and C in there?

\* \* \*

Q. You never saw that patent prior to the [331] time you designed the defendant's Paramount fixture, did you? A. This patent?

Q. Yes. A. I have never seen that before.

Q. And look at C of the same exhibit. Did you ever see that patent—— A. No, sir.

Q. ——before you made your design?

A. No, sir.

(Testimony of Benjamin Ruby.)

Q. Did you ever see a fixture having exactly the design of tab C before you made your design?

A. I have seen this before.

Q. Did you ever see a fixture having exactly the design of tab B before you?

A. Which is that?

Q. This one (indicating).

A. This one,—I have seen several shapes of fixtures like that.

Mr. Miketta: You have seen that?

The Witness: I have seen some shapes of fixtures like that when I was in New York.

Q. (By Mr. Foster): Have you seen a fixture having exactly the design of the patent tab B of Plaintiff's Exhibit 10? A. Which is B? [332]

Q. This (indicating). A. The patent?

Q. Have you seen a fixture having exactly that design? A. Close to it; very close to it.

Q. I direct your attention to tab AH, and ask you if you ever saw that patent before you made the design of the Paramount fixture, Plaintiff's Exhibits 14 and 15? A. This patent?

Q. Yes.

A. I have never seen that before.

Q. Have you ever seen, before you made your design, tab AM? Have you ever seen that patent?

A. No, sir.

Q. Did you see the patent AU before you made the design of the Paramount fixture?

A. No, sir.

(Testimony of Benjamin Ruby.)

Mr. Foster: The patents to which I have called attention in Plaintiff's Exhibit 10, your Honor, are the patents pleaded by the defendant as anticipating the patents in suit.

Q. (By Mr. Foster): Now, I direct your attention to the other book there before you, which is Plaintiff's Exhibit 9, and, particularly to the catalog which is tab B of that exhibit. Did you have those catalog sheets, tab B, before you, or use them in making the design on the Paramount [333] fixture?

\* \* \*

A. No, sir, I have never seen them.

Q. —before making the design?

A. I have never seen them, no, sir.

Q. Then turn to tab C. Did you have before you that sheet?

A. I have never seen this before.

Q. And tab D, Illuminating Engineer. Did you ever see that before?           A. No, sir.

Q. Tab E, another Illuminating Engineer page. Did you ever see that before?           A. No, sir.

Q. Tab F, catalog of Guth Company.

A. Guth.

Q. Did you ever see that before?

A. No, I haven't seen this fixture.

Mr. Foster: Those are the catalog sheets in [334] Plaintiff's Exhibit 9, your Honor, which have been pleaded by the defendant as anticipating the design of the patent in suit.



(Testimony of Benjamin Ruby.)

The Court: Is it true, counsel, that knowledge doesn't make too much difference in these matters?

Mr. Foster: That is true, your Honor.

\* \* \*

The Court: The statement I made should be, more accurately, if a design or patent is actually anticipated, it doesn't make any difference whether the party knew first-hand that it was so anticipated or not?

Mr. Foster: Yes, I agree with that, your Honor. I think that is the law. [335]

\* \* \*

Q. (By Mr. Foster): When you were developing the design of the Paramount fixture, Plaintiff's Exhibits 14 and 15, did you utilize what was shown by any patents in that work? A. No, sir.

Q. Or any catalogs I have shown you?

A. No, sir.

Q. The defendant corporation sells its lighting fixtures to the same class of people to whom the plaintiff corporation sells its lighting fixtures, Plaintiff's Exhibit 13, that is true, isn't it?

A. Approximately the same.

\* \* \*

The Court: Are you in competition? You have seen the [337] plaintiff's device, which is Exhibit 13, and you have seen your devices, which are Exhibits 14 and 15. Is your company in competition with the plaintiff in connection with the sale of those devices?

(Testimony of Benjamin Ruby.)

The Witness: Yes, sir, with an explanation.

The Court: What is your explanation?

The Witness: They have a certain clientele that won't buy my fixture, and I have a clientele that won't buy theirs. I can give you an example. They sell Graybar Company that fixture. I can't sell it to them. I may sell Westinghouse, and they won't buy theirs. But it is the same line of business.

Mr. Foster: Have you finished, your Honor?

The Court: Yes.

What is the relative price of these two fixtures, or is that material?

Q. (By Mr. Foster): For what price do you sell the two-lamp Paramount fixture and the four-lamp? A. For what price we sell it?

Q. Yes.

A. It is in my price list here. Have you got a price list?

Q. I show you Plaintiff's Exhibit 9. Is it in any of those catalogs?

(A document was handed to the witness.) [338]

The Court: Which is the two-lamp, Exhibit 14 or 15?

Mr. Foster: Plaintiff's Exhibit 14.

The Witness: \$33.80, less 50 and 10. \$33.88, less 50 and 10.

Q. (By Mr. Foster): Less 50 per cent and then less 10 per cent?

A. Yes, that's right. It is 50 and then less 10.

Q. Which Paramount fixture is that?

(Testimony of Benjamin Ruby.)

A. The two-light.

The Court: What is the 50 per cent discount? To whom?

The Witness: That is the jobber. He gets 50 and 10, and then the jobber resells it less 50 or 40 off, and they make the difference.

Q. (By Mr. Foster): Is the two-lamp a surface-attached lamp or a suspended lamp?

A. Everything on the price list is without hangers. Just surface mounted.

Q. And the four-lamp?

A. The price of the four-lamp is \$48.88.

The Court: That includes the fluorescent lamps?

The Witness: No. We don't sell lamps.

\* \* \*

The Court: Is there a stipulation as to what [339] plaintiff sells No. 13 at?

Mr. Foster: May we have your indulgence here a moment, your Honor, and I will show it to Mr. Miketta?

Plaintiff's Exhibit 13, their fixture, the two-tube surface light has a list price of \$41.40, less 50 per cent and less 20 per cent, making a net of \$16.56, freight allowed.

The Court: That is surface attached?

Mr. Foster: Yes. That is to be compared with the defendant's net price of \$15.25.

The Court: The defendant's net?

Mr. Foster: Yes, \$15.25.

The Court: Is it stipulated that is what \$33.88 minus 50, minus 10, would figure out, \$15.25?

(Testimony of Benjamin Ruby.)

Mr. Miketta: So stipulated, your Honor.

Q. (By Mr. Foster): In general, as I understand it, Mr. Ruby, the defendant corporation competes with the plaintiff corporation in the sale of its Plaintiff's Exhibits 14 and 15, the Paramount fixture?

A. Yes, sir.

Mr. Miketta: May I interrupt for a second while we are talking about price, your Honor? Mr. Ruby's price is f.o.b. factory, whereas the plaintiff's price is on a freight-allowed basis.

Mr. Foster: That is correct. [340]

\* \* \*

The Court: What do you mean by the plaintiff's price, "freight allowed"?

Mr. Miketta: I think the meaning of that is that the company, the plaintiff, pays the freight to its destination.

Mr. Foster: That is the effect of it. The customer pays the freight and we give him credit for the freight paid in billing him. We allow it. That is the reason for the word "allowed."

\* \* \*

### Cross-Examination

By Mr. Miketta:

Q. Mr. Ruby, when did you first start working on lighting fixtures?

A. Working in the industry, is that it?

Q. Yes. A. About 1915.

Q. You were quite a young man then, weren't you?

A. Fourteen years old. [341]

Q. When did you first engage in the business or



(Testimony of Benjamin Ruby.)

have your own business in which you were manufacturing lighting fixtures?      A. In 1925.

Q. That was in New York?      A. Yes.

Q. That was called the Ruby Lamp Manufacturing Company.      A. That is correct.

\* \* \*

Q. (By Mr. Miketta): I show you Defendant's Exhibit B for identification and ask you to tell us what that is.

A. That is the Ruby lighting catalog.

Q. For what year?      A. 1939.

Q. Does this illustrate the various designs of lighting fixtures which your company was manufacturing in 1939?      A. That is correct.

Q. Prior to 1939 what types of fixtures [342] were you manufacturing?

A. We manufactured incandescent and what they call lumiline.

Q. That meant a long incandescent bulb?

A. Long incandescent bulb.

Q. During the course of your work prior to 1940 or '42, had you personally engaged in, you may say, manufacturing activities like metal cutting and bending and welding in various plant operations?

A. Prior to 1925 I worked in a factory, in the industry.

Q. So you are familiar with production methods and how to handle tools?      A. Yes, sir.

Q. During the course of those years from, say, 1925 to 1942, had you made yourself familiar with

(Testimony of Benjamin Ruby.)

the catalogs published by other manufacturers of lighting fixtures?

A. Well, we would get catalogs, and my associates used to take care of that end of it. I was the factory man at that time.

Q. But you have seen numerous catalogs?

A. Yes, surely.

Q. Have you ever done any sales work?

A. Partly, yes, sir.

Q. You are familiar with what the trade desires in the form of lighting fixtures, aren't you? [343]

A. Yes, sir.

Q. And you were familiar with the desires of the trade in, say, 1942, '43, '44? A. Yes, sir.

Q. And before you designed the defendant's fixtures? A. Yes, sir.

Q. That are in suit here? A. Yes, sir.

Q. In talking about Exhibit 19, which is that single sheet, you said something about a labor saving that you made in the factory.

A. That is correct.

Q. Will you please explain what you were talking about? What labor saving?

A. I have saved four spot-welds on each side of the fixture.

Q. By doing what?

A. By making that little oval design.

Q. In other words, by eliminating the three bars shown on Exhibit 19 and substituting in its stead the medallion which is shown on page 9 of Exhibit 18 you saved four spot-welding operations?

(Testimony of Benjamin Ruby.)

A. Yes. Eight for a complete fixture, both sides, four on each side.

Q. So that that medallion is now spot-welded only in [344] two places, to the top and the bottom rail on each side, is that correct?

A. That's correct, yes.

Q. As exemplified by Plaintiff's Exhibits 14 and 15 in the courtroom, is that correct?

A. That is correct. Are 14 and 15 my fixtures?

Q. Yes. A. That's right.

Q. That change that you made, then, was a change for purposes of economy, is that correct?

A. Correct.

Q. And it did not affect the light distribution, is that correct?

A. Not at all.

Q. Prior to 1946, did you supervise the activities of your salesmen?

A. I did.

Q. Do you receive bids from various governmental bureaus like the Division of Architecture of the Department of Public Works, and the Army and the Navy, and other people who are interested in building?

A. Yes, sir. [345]

\* \* \*

Q. (By Mr. Miketta): Mr. Ruby, when we talk about specifications or requests for bids, in general, you are familiar with various specifications and requests?

A. Yes, sir.

Q. Is it customary in such specifications and bids, which you may have received at any time during the past ten years, to specify a particular design or ornamentation on a fixture?

(Testimony of Benjamin Ruby.)

A. No, sir.

Q. Is it customary in specifications for fluorescent lighting fixtures to specify the wattage of the fixtures?

A. Yes, sir.

Q. Is it customary that those specifications specify cut-off angles? [347]

A. Yes, sir.

Q. And characteristics of a ballast or reactor to be used?

A. Yes, sir.

Q. And do such specifications, in general, tell you whether they are going to be surface hung or provided with hangers?

A. Yes, sir.

Q. But they don't specify whether the fixture should have inclined sides or a flat bottom, or whether it should be of one design or another, do they?

A. No, sir.

Q. In general how do these specifications identify the fixture that the purchaser wants to buy?

A. Well, they will put in the specifications "Benjamin or equal," that is a make, "Miller Company or equal," "Day-Brite or equal," "Ruby or equal," but nothing about style, shape of fixture. They will tell you 30-degree or 40-degree, or so much up-light, so much down-light.

Q. And requirements of that type to which you have referred are illustrated in Defendant's Exhibit C, for identification?

A. Yes, sir. [348]

\* \* \*

The Court: \* \* \* Are you going to offer in evidence Exhibit B?

Mr. Miketta: Yes, I would like to have that in



(Testimony of Benjamin Ruby.)

evidence, your Honor. May I now offer it in evidence. [349]

\* \* \*

The Court: It will be admitted into evidence as Defendant's Exhibit B.

\* \* \*

Q. (By Mr. Miketta): Now, Mr. Ruby, you testified that you did not have before you at the time that you were working on the design, the defendant's Paramount fixture which is before this court as Plaintiff's Exhibits 14 and 15,—that you did not have before you at that time certain specific fixtures in Plaintiff's Exhibit 9 or certain prior patents shown in Plaintiff's Exhibit 10. Was that your testimony? A. That's right.

Q. But you did have a background of experience in which you had seen a good many of those fixtures, have you not? A. Yes, sir.

Q. Now, prior to the time that you and Bob worked on this design of the Paramount fixture, had you seen fixtures similar to those illustrated in Plaintiff's Exhibit 9, tab B? A. Yes, sir.

Q. And certain of those fixtures had step-down and perforated ends, did they not? [351]

A. Yes, sir.

Q. And most of them had inclined translucent sides; is that correct? A. Yes, sir.

Q. And some had louvers, and some didn't have louvers? A. Yes, sir.

Q. And in some the side panels were divided by some sort of a banding, and in others, they were not; is that correct? A. That's correct.

(Testimony of Benjamin Ruby.)

Q. You knew the trend in which the art, if you can call it an art, the desires of your purchasers were going; is that correct? A. Yes, sir.

Q. Did they want lighter-looking fixtures or heavier-looking fixtures? A. Lighter-looking.

Q. So in your design you tended to make your fixture as compact as possible; is that correct?

A. Correct.

Q. I understood you to say that you started business in Los Angeles about 1940 or '42?

A. '40, sir.

Q. In 1940?

A. Or in late '39, it may be; approximately. [352]

Q. At that time, Mr. Ruby, was there any other company engaged in the manufacture of fluorescent fixtures in the Los Angeles area?

A. Not that I know of.

Q. Since then are there other companies engaged in the manufacture of fluorescent fixtures?

A. Lots of them.

Q. Can you name some of them?

A. Well, the Sunbeam is a large company; they are former employees of mine. I can't name all of them. Let me see. The Sunbeam, and there is Lumidor, and Smoot-Holman makes lighting fixtures, fluorescent.

Q. Are they engaged in manufacturing fixtures that are similar to the Paramount fixture?

A. Yes, sir.

Q. You state that some of your employees are now associated with the Sunbeam?

(Testimony of Benjamin Ruby.)

A. Yes, that's the Sunbeam Company. I brought them here from New York.

Q. When did they leave you?

A. About two years later; I would say in '44.

The Clerk: I have marked three documents Defendant's Exhibits D, E and F, for identification.

The Court: D, E and F. [353]

\* \* \*

Q. (By Mr. Miketta): I show you three catalogs marked Defendant's Exhibits D, E and F, for identification, and ask you to point out any fixtures illustrated therein which, to your mind, are rather similar to those which form the subject-matter of the action here.

A. There is one right there (indicating).

The Court: Just a moment. You are talking about Exhibit D, for identification?

Mr. Miketta: Yes, on Exhibit D.

The Court: All right.

Q. (By Mr. Miketta): And you are pointing to——

A. 1204; L 1204.

Q. A fixture known as L 1204?

A. Yes. That's better than mine.

Q. Now, you are referring to Exhibit E?

A. Let's see. There's one close to it. This one here (indicating).

Q. Now, you are pointing to page 8 of Exhibit E, an item in the upper left-hand side marked L 1210-SL series. Do you consider that lamp to be similar to the lamps——

(Testimony of Benjamin Ruby.)

A. Yes, sir.

Q. —forming the subject-matter of this action?

A. Yes, sir. There's another one (indicating). [354]

Q. Another one on page—what page is that?

A. Page 4.

Q. On page 4, the fourth lamp from the top of the page; is that correct? A. Yes, sir.

Mr. Foster: What number is that?

The Witness: That is L 1210.

Mr. Miketta: L 1210.

The Court: Let me see it before you lose it.

(The document was handed to the court.)

Mr. Foster: May I interrupt to ask: All of these catalogs, D, E, F, for identification, are subsequent to the patents in suit, are they?

Mr. Miketta: I have not looked at the dates.

Mr. Foster: They are not offered as prior art, though?

Mr. Miketta: May I check the dates on them?

Mr. Foster: The witness testified the Sunbeam did this.

The Witness: Two years later.

Mr. Foster: —after this, so they are not prior art at all, as I understand it?

The Witness: That is right.

Mr. Miketta: I think that is correct.

The Court: Defendant's E on the front page, the first insert page, states "Effective June 1, 1949." That is this schedule. [355]



(Testimony of Benjamin Ruby.)

Mr. Miketta: These exhibits, your Honor, are simply offered for the purpose of indicating what the trade, what the manufacturers are making, and what the public desires in the form of lighting fixtures.

Mr. Foster: But all subsequent to the date of the patents in suit?

Mr. Miketta: They are subsequent to the date of the patent in suit, as far as the specific items referred to by the witness, counsel.

The witness also has referred to Exhibit F, for identification, and particularly to page 5, which illustrate the 1210 series again, your Honor.

The Court: Are you offering these?

Mr. Miketta: Yes, your Honor. I am offering those in evidence for the purpose of indicating the character of fixtures that are being manufactured, and the similarity of those fixtures to prior art designs.

Mr. Foster: I think it is immaterial, your Honor, and, certainly, it is not prior art and is confusing in the record. It is objected to on that ground, all being subsequent to the date of the patents in suit.

Mr. Miketta: I admit that the publications are subsequent, but I think they can be tied in with Mr. Ruby's 1941 catalog, and the same representations which appear there also are to be found in Defendant's Exhibits now being [356] offered in evidence.

Mr. Foster; Is it the defendant's position that this 1210 design of Exhibit F is the same as the defendant's design? Is that it?

(Testimony of Benjamin Ruby.)

Mr. Miketta: Very similar, and similar to others in the 1941 catalog.

The Court: In view of the limited scope of the offer, there is no harm in admitting them. It is conceded it is not prior art?

Mr. Miketta: That is right, your Honor.

The Court: The objection will be overruled. They will be admitted into evidence as Exhibits D, E and F. [357]

\* \* \*

Redirect Examination

(Resumed)

By Mr. Foster:

Q. Mr. Ruby, in the production of the Paramount fixture, Plaintiff's Exhibits 14 and 15, as compared with Paramount fixture shown in Plaintiff's Exhibit 19, you save four spot welds on each side of the fixture with regard to the decoration of the metal of each side, is that correct?

A. I said I saved four. It would be six, instead of two.

Q. Do I understand that in the production of the fixture of Plaintiff's Exhibit 19 there were six spot welds on each side?

A. There would be six, I said.

Q. And there are two on each side of the Plaintiff's Exhibits 15 and 14, is that correct?

A. That is correct.

Q. That decorative medallion in the middle of the side of the Paramount fixture, Plaintiff's Ex-

(Testimony of Benjamin Ruby.)

hibits 14 and 15, [259] is stamped out of one piece of metal, isn't it?           A. That's right.

Q. And at the top of each and the bottom of each there are two spot welds to the side rail?

A. Correct.

Q. Couldn't the decorative medallion in the middle of each side of plaintiff's Exhibit 19 indicated by the pencil numeral 1 be stamped out of one piece?

A. Not all three of them.

Q. Why not? What is there that is an obstacle to making that a metal stamping just as it is a metal stamping in the middle of the side of Plaintiff's Exhibits 14 and 15?

\* \* \*

The Witness: I didn't know how to make it all in one. [360]

Q. (By Mr. Foster): Have you had experience now with making fixtures that enables you to state whether or not the decorative medallion in the middle of the sides of the fixture, Plaintiff's Exhibit 19, could be stamped in one piece?

A. No, sir.

Q. Were you influenced, Mr. Ruby, in changing the design of the medallion in the middle of each side of the fixture, indicated by the pencil numeral 1 on Plaintiff's Exhibit 19, by a desire to get further away from the plaintiff's designed fixture,—

A. No, sir.

Q. —Plaintiff's Exhibit 13?

A. No, sir.

(Testimony of Benjamin Ruby.)

Q. Well, is it your testimony to the court that you had not seen the plaintiff's Viz-aid fixture, Plaintiff's Exhibit 13, when you made the change in design in—— A. I didn't——

Q. ——Plaintiff's Exhibit 19?

A. I didn't pay attention to the Viz-aid. I have seen a lot of fixtures together.

Q. You don't want to have your testimony show that you had not seen a Viz-aid Day-Brite fixture like Plaintiff's Exhibit 13 before you made this change of design in Plaintiff's Exhibit 19? [361]

A. I didn't know three years ago there was a Viz-aid. I have seen a lot of fixtures in a group.

Q. Had you or had you not seen the plaintiff's Viz-aid fixture, Plaintiff's Exhibit 13, before you made this change in your design?

A. Before I made this design?

Q. Yes.

A. I couldn't remember exactly. I don't think I have seen it. I won't say "Yes," and I won't say "No."

Q. Now, I direct your attention to Defendant's Exhibit F, and to page 5 thereof, showing the 1210 series of Sunbeam, and to Defendant's Exhibit E, page 11, showing the L 1210 series fixture of Sunbeam. It is a fact, isn't it, that some employees of yours formed or went to work for the Sunbeam Company? A. They formed it. [362]



(Testimony of Benjamin Ruby.)

Q. Well, do you regard this 1210 series of the Sunbeam light fixtures, which I have identified in Defendant's Exhibits E and F, as being a copy of your fixture, Plaintiff's Exhibits 14 and 15?

A. No. I would say it is a similar fixture.

\* \* \*

Q. Do you think this Sunbeam fixture, 1210, for identification, is in its over-all appearance, general appearance, eye appeal, substantially the same as your Paramount fixture?

\* \* \*

A. Not the same, but they look close. [363]

\* \* \*

Q. Well, do you think that an ordinary purchaser, giving ordinary attention to the Sunbeam fixture 1210 I have identified, would be confused into thinking that was the same as your Paramount fixture?

A. I don't think so. [364]

\* \* \*

Mr. Foster: Therefore, at this time, it can come as nothing new that the plaintiff moves for leave of court, pursuant to the federal rules, to amend its complaint to conform to the evidence, by adding to the two counts contained in the original a third count, which I proffer, which alleges, in general, the creation of a market and demand for the patented product, and the appropriation of that market as unfair competition both in aggravation of damages

from the patent infringement and as a wrong in itself. So that this time the plaintiff moves for leave to file a first amendment to its complaint. [367]

\* \* \*

So that I urge upon your Honor that the amendment sought to be made by this motion introduces no new issues in the case, it requires no new evidence to support it, and can therefore be subject to no valid objection by the defendant. The same acts that constitute the patent infringement constitute support for the allegation of wrong contained in this first amendment, the subject of this motion. [368]

\* \* \*

Mr. Foster: Your Honor, I have no objection if the court prefers to take the motion under submission. We have no additional evidence to present. The plaintiff has put in its proof and is hereby closing its prima facie case. [372]

\* \* \*

The Court: When did you first decide you were going to set forth a cause of action of unfair competition? [378]

\* \* \*

Mr. Foster: I cannot represent to your Honor that I did not entertain the thought of the possibility of an amendment earlier than the commencement of the trial, however, because I had considered it, and considered the fact that the evidence would be the same. But I did not know whether there would be evidence, sufficient evidence, of copying to

warrant the support of the charge of copying. [379]

\* \* \*

MILTON B. GROSSMAN

called as a witness by and on behalf of the defendant, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name, please?

The Witness: Milton B. Grossman.

Direct Examination

By Mr. Miketta:

Q. What is your business or occupation, Mr. Grossman?

A. I am an electrical engineer in the illumination field, and I also do industrial design.

\* \* \*

Q. Have you been previously in the employ of the defendant to this action? [388]

A. Yes, sir.

Q. Ruby Lighting? A. Yes, sir.

Q. Will you please tell us what was your first experience in the lighting field, when it occurred, and what were your duties?

A. I did industrial design back in New York in connection with Central Buying Offices, which managed, operated, and purchased equipment for retail stores, department stores, specialty stores. I had the job of working on store layout, store air-conditioning, store illumination, assisting buyers in the selection of equipment, the appearance of equip-

(Testimony of Milton B. Grossman.)

ment, calling for changes of equipment to meet certain requirements, and in general what is now termed industrial design in the retail field.

Q. During what years were you so occupied with the Central Buying Offices?

A. From about 1932 to 1942.

Q. Prior to 1932 what did you do?

A. I was in merchandising work, marketing and merchandising work.

Q. What did you do between 1942 and, say 1947?

\* \* \*

A. From 1942 to 1945 I was in the Army, [389] France, Belgium, E.T.O.

Q. When did you return from service?

A. 1945, October. 1945 to 1947 I was here in L. A. attending USC and also working as an engineer and industrial designer, getting my degree at USC.

Q. You are familiar with fluorescent tube fixtures, I take it?

A. Yes, sir.

Q. Approximately when were fluorescent tube fixtures first employed commercially or fairly extensively?

A. Well, the inception of the presentation commercially of fluorescent tubes occurred, to the best of my recollection, at the World's Fair in 1939.

\* \* \*

Q. Do fluorescent tubes come in any specified sizes or standardized sizes or lengths?

A. Yes, they do. The ones that have been con-



(Testimony of Milton B. Grossman.)

cerned in this case come in lengths running from six inches on up to 96 inches, in units—not units, but running pretty much six inches, 14 inches, 18 inches, 24 inches, 33 inches, 36 inches, 42 inches, 48 inches, and on up.

Q. Have you ever sold lighting fixtures? [390]

A. Yes, I have.

Q. Have you sold fluorescent lighting fixtures?

A. I have sold them in terms of doing the sales engineering work connected with it, yes.

Q. With whom did you perform the sales engineering functions for these fixtures?

A. Architects, engineers, designers, state, county and city, federal purchasing officials and their respective engineers, purchasing agents of wholesale jobbers, and also the purchasing agents of contractors.

Q. Over what period of time would you say that this sales engineering work of yours has been carried out?

A. In fluorescent tubes alone, sir?

Q. Yes.

A. From the time I was out here, about, say 1947 or so.

Q. In selling fluorescent lighting fixtures what do you find to be the important criterion or criteria which your purchasers seem to be interested [391] in?

\* \* \*

The Witness: If I had to phrase it in one word, I would say illumination efficiency. But the criteria are many-fold and they consist of items such as

(Testimony of Milton B. Grossman.)

shielding, surface brightness of certain sections, method by which the light is distributed, as to whether the unit is totally indirect, totally direct, semi-indirect and so forth, categories that have been established in rather rigid channels by such sets of valuations as Fleur-O-Lier and RLM specifications, specifications as to the strength and type of material from which the unit is made, transmission qualities of those parts of the unit that are either translucent or transparent, reflective qualities of those parts of the units or finishes of the units that are impinged on by light coming from the illuminating source, mechanical operational factors that would make for ease of maintenance, removal of tube, ease of cleaning of the unit, mechanical features that would make for long life in terms of handling of the unit by the average maintenance man [392] or janitor, stability of structure of the unit, and possibly 15 or 20 other functional specifications that have appeared in the Fleur-O-Lier specs or RLM specs, depending on what type of unit it is, or that have appeared in government specs, and which are the basis and the criteria used by those who either specify or purchase fluorescent fixtures. ETL—do you want me to continue?

Q. Have you finished your answer?

A. No. ETL test values, such as distribution patterns, coefficients of utilizations, angular dispersions, percentages upward or downward, cut-off angles, absence of glare points. I think that would be enough for the moment.

(Testimony of Milton B. Grossman.)

Q. You mentioned ETL reports. I hand you a copy of Defendant's Exhibit H, for identification. Will you please state what that is?

A. It is a reproduction of an electrical testing laboratory report showing the candlepower distribution of Ruby No. 302 unit tested in a suspension mounted condition, and it is given the title of general diffuse type of fixture. It shows a set of distribution curves on three axis used for the tests. It shows brightness factors for the different angles and different positions; it shows zonal distribution and zonal lumens; it shows light flux values and efficiencies, and it indicates the general form of the fixture in its cross-sectional outline, although the dimensions are incorrect. [393]

Q. You are familiar with this report?

A. Yes, sir.

Q. And this Ruby Fixture No. 302 is the type of fixture which is here as Plaintiff's Exhibit 14 and 15, similar to the one on the standard?

A. It is.

\* \* \*

Mr. Miketta: I wish to introduce Defendant's Exhibit H into evidence, your Honor.

\* \* \*

The Court: The objection is overruled and the document is admitted as Defendant's Exhibit H.

\* \* \*

Q. (By Mr. Miketta): You have utilized ETL

(Testimony of Milton B. Grossman.)

reports similar to Defendant's Exhibit H in your sales engineering work, Mr. Grossman?

A. Yes, sir.

Q. Do you find that such reports indicating the light distribution and other factors to which you have referred are important in making sales of fixtures?

\* \* \*

The Witness: It has been my experience in the last two years that not only are they important, but they are the prime key in the acceptance and specification of lighting fixtures today.

Q. (By Mr. Miketta): In the course of your work with [395] Ruby Lighting Corporation did you have anything to do with the plaintiff's Exhibit 20? A. Yes, sir.

Q. What did you do in connection with that?

A. I wrote, laid out, and designed and supervised the production of that entire data book.

Q. So that you are familiar with all of the fixtures that are illustrated, described and shown in this publication, is that correct?

A. Yes, sir.

Q. I believe in the course of your testimony you had reference to specs. What did you mean by "specs"? A. Specifications.

Q. Specifications of purchasers?

A. Specifications set down either by the purchaser or set down by accepted organizations such as the Fleur-O-Lier specification set-up or the Bureau of Standards, or the Illuminating Engineers



(Testimony of Milton B. Grossman.)

Society in their sets of specifications for different types of uses of fixtures.

Q. And do those specifications concern themselves with decorative or ornamental features of fixtures, or only with the functional and mechanical features?

A. Only with the functional and mechanical. [396]

\* \* \*

Mr. Miketta: If the court please, the exhibit which I have asked be marked for identification as Exhibit I is a collection of both design patents and mechanical patents relating to fluorescent lighting fixtures. Copies of these patents have been, of course, furnished to counsel for the plaintiff. It also includes under tabbed items photostatic copies of various publications, including the *Illuminating Engineering*, which also appears in some other exhibits, and a "Review of Fluorescent Luminaire Design" under the tab No. 21. I believe in view of the written stipulation which we have, Mr. Foster, that that exhibit can be admitted in evidence.

\* \* \*

Mr. Foster: As to the book of prior patents and publications offered by the defendant, my objections for the record are two in number. One, that with respect to most [397] of the items, they are already in evidence, your Honor, in Plaintiff's Exhibits 9 and 10. They include all of the prior patents and catalogs that were pleaded by Mr. Miketta, or con-

(Testimony of Milton B. Grossman.)

cerning which he had given me notice prior to trial. The other prior patents, and they are only two that aren't already in evidence, and prior catalogs,—their use is objected to if they are to be relied upon as anticipating the patents in suit and establishing invalidity because no 30-day notice was given the plaintiff by pleading, as required by statute. If they are not to be relied upon as anticipating, that is, fully showing the designs of the patent in suit, but only to show the state of the art, the general art, and to enable a contention to be made that no invention is involved, then the plaintiff does not object to those additional ones, but objects to all of them, in that the material ones, the best ones for the defense, are already in the record.

The Court: No 30-day notice was given, was it?

Mr. Miketta: That is correct. And I do not contend that any of these patents actually anticipate the entire design patent in suit, but I offer them to show the state of the art.

Mr. Foster: We do not urge surprise at all, your Honor.

The Court: All right. Exhibit I will be admitted, and although there is a duplication in some of the patents, in the [398] patents contained in this exhibit I notice Mr. Miketta has marked and underlined certain portions of the patents to make readily apparent what parts he relies upon. In that sense it would be of some assistance to have this exhibit, from the standpoint of his contentions, as

(Testimony of Milton B. Grossman.)

well as the duplication of the patents from your standpoint. [399]

\* \* \*

Q. (By Mr. Miketta): Mr. Grossman, based upon your knowledge of fluorescent fixtures, can you state whether 2-tube fixtures as of 1942 were commonly made? A. Yes, they were.

Q. And if you refer now to Exhibit I, item 21, which is the Review of Fluorescent Luminaire Design, imprinted from the Magazine of Light of 1940, will you point out the characteristics of fixtures which are similar to or include elements which you find in the defendant's Paramount fixture?

A. Well, on page 6, entitled, "A Review of Fluorescent Luminaire Design" on the left-hand side there are four illustrations of fixtures. The bottom one shows a fixture that typifies elements such as also are found in the Paramount fixture. For instance, there is a step-down end, as I have marked it with these notations. Then the end itself has cut-outs so that a certain amount of illumination is escaping from the end of the fixture. The fixture itself, based on the cross-section drawing, shows a "V" center reflector to aid in the cut-off or shielding of the outside tube when seen from the other side of the fixture. In the [400] bottom conformation of the fixture are seen the baffles of the fixture, and what we call in the trade the off-horizontal. It seems to be curved here, and it is typical of the curved or angular bottom, off-horizontal bottom used in the sectioning of the baffles.

(Testimony of Milton B. Grossman.)

Q. Does that Exhibit I-21, page 6, and particularly the lower item, include any comments which explain why the step-down end, as you called it, is important or functional?

A. Why, yes. It states very definitely that "The plastic sides and central member furnish shielding for crosswise view. The louvers shield for lengthwise view. The design of the upper part of the reflector is such as to direct light to the ceiling, thus eliminating objectionable ceiling contrasts." [401]

Q. What is meant by that last phrase or description, Mr. Grossman?

\* \* \*

A. If the fixture is mounted as, for example, is the one in the court room, and were to be lit up and had a sharp contrasting differentiation between the brightness of the fixture itself and the ceiling, it would tend to become an object of glare to the eyes of a person that was in the room and using that fixture.

As a result, fixture design has attempted to eliminate that so that there is a gradation of brightness from the side or bottom surface to the brightness of the ceiling, the adjacent ceiling, somewhat in the ratio of three to one. When it gets beyond that ratio, it is considered as having a bad quality.

The Court: Which is the three,—the downward?

The Witness: The side or the bottom, sir. They take——

The Court: And one is the ceiling? [402]

The Witness: Yes, sir.



(Testimony of Milton B. Grossman.)

Q. Well, in designing a fixture, do you attempt to do anything about maintaining that light on the ceiling, even though a number of fixtures are placed in alignment?

A. Oh, yes. It is maintained by dropping the side surface so that there is some light leak either over the edge of the fixture or from the body of the fixture, or, sometimes, as in the case of the fixtures that have baffles on the top or reflectors on the top so that there isn't any direct path of light from the tubes to the adjacent ceiling, they have slots so that a certain amount of light can get to the ceiling.

Then in other cases, if you will note, for instance, as advertised by the Guth Company, which they have used for years [403] back to the acetylene, sir, they have what they call a bottom spill that shoots light to the ceiling from the bottom of the side.

Q. So that the step-down end itself has a tendency to transmit light lengthwise of the fixture against the ceiling?

A. Very definitely, as you can see from here.

Q. And, also, over the edge towards the side of the fixture; is that right?

A. Yes. And it is not only that, but that step-down is almost a requirement on fixtures of this nature. But when a test is made in electrical testing laboratories, the test is made on three planes; on a plane—that is, the fixture is located in a plane parallel with the longitudinal axis; also, in a

(Testimony of Milton B. Grossman.)

plane at right angles with the longitudinal axis; and a plane at 45 degrees to the longitudinal axis. The result is that if they didn't have a step-down on the ends of the fixture, when the test report would be evaluated in terms of zonal lumens, which you use for the computation of efficiency, the values of light that would now be seen or could be seen in fixtures like this, coming from the sides and the ends, would not appear on the tests, and the fixture would be relatively an inefficient fixture.

Q. Is it also true, Mr. Grossman, that the overall length of the fixture is made as close to the length of the [404] tube that is contained in the fixture in order to prevent dead spots, you may say, or dark spots between adjacent fixtures, when they are in alignment? A. Yes, sir. [405]

Q. Do you find any other instances where V-shaped longitudinal louvers have been combined with transverse louvers in prior suggestions as shown in Exhibit I-21?

A. Yes, sir, on page 8, the bottom fixture on the left-hand side shows V-shaped lengthwise louvers.

Q. As well as transverse louvers?

A. As well as transverse louvers, sir.

Q. Do you find any other instance of prior fixtures which embody some of the characteristics of the defendant's fixture in Exhibit I-21?

A. Yes. On page 10, the upper left-hand fixture indicates very much what I just discussed. It has a step-down end. Of course, that step-down isn't

(Testimony of Milton B. Grossman.)

required so much when it is on a pendant like that. But if that fixture were hung on a ceiling it would be required. It also shows a cutout and permits some light to come through.

I see I made a notation on this. The second fixture in that column on page 10 shows a typical bracing of the side, reinforcing straps on the side, straps that hold the panels on the side.

Q. Between the upper and lower rails?

A. Yes, sir. And on page 13 there is a V-shaped fixture which again indicates the step-down end, the cutout end, and side reinforcement of the sustaining rails or bands for the side panel. That is the one on the upper left. [406]

The Court: On page 13?

The Witness: Yes. The second one down on the right on that same page indicates illuminated end cutouts. And I notice that I made a notation here of arrow-tail form.

Q. (By Mr. Miketta): What do you mean by that?

A. That in terms of a resulting pattern that results from the form—the functional form of getting two pieces of glass and then putting an end cap on it and, bang, you have an outline of an arrow which results purely from the function.

Q. What is the function of the inclined sides?

A. In order to get luminous surfaces at an angle off the perpendicular.

Q. What does that accomplish?

(Testimony of Milton B. Grossman.)

A. It accomplishes a better transmission of light to the working surface.

Q. Do you mean downwardly?

A. Downwardly. Insofar as the light is directed proportional to the cosine of the angle between the vertical and the normal to whatever the plane is. If the angle were closer to 90 degrees or vertical, the efficiency of that surface in delivering light to a horizontal working surface would be that much lessened.

I notice also on page 14 the second fixture down on the right, under the Fleur-O-Lier label, Electrical Testing Laboratory label, it also has a step-down end, it has a cross-section [407] that is identical to the type of cross-section that the Ruby fixture has, and it has bracings or straps on the side, middle, between the upper and lower railings, holding the fixture panel; and on page 15 on the left-hand side, the second illustration, there is a fixture that shows a step-down end, it shows a textured surface on the end that very much uses the kind of texturing that we use on the casting of the Ruby end insofar as it incorporates a floral pattern and an indented, different surface, and on top of that has cutouts evidently for the same reason that we most likely have, I can speculate, to save metal and to permit light to come through the end of the fixture. Those are the notations I see.

Q. Mr. Grossman, it is my understanding from testimony given here previously and from your description, that every fixture has to distribute light,



(Testimony of Milton B. Grossman.)

that is its primary function, and it has to distribute it in various directions, that the louvered bottom performs the function of preventing glare, the inclined sides direct the light downwardly, the space between the upper edges of the side permits light to be cast upon the ceiling, the step-down end of the fixture permits light to be thrown against the ceiling, the length of the fixture is a function of the tube length; do you find any element of a fixture which I have not named and which is not functional?

A. I don't like the way, frankly, you phrase it, Mr. [408] Miketta. Do you mean the result of a function?

Q. Do all those elements or angles perform a function or purpose which aids in the distribution of light from the fixture?

A. Yes, sir, they [409] do.

Q. Now, in addition to that, you do find some ornamentation applied to the end of most of these fixtures, do you not?

A. Yes, that is the end factor.

Q. And as I understand your testimony, the ornamentation which appears in the defendant's fixtures in the form of those cut-outs is also, at least partly, functional in that it permits light to be distributed towards the end of the fixture?

A. Yes, sir.

Q. And pass through those ends, is that correct?

A. Yes.

Q. Mr. Grossman, do you know the range in

(Testimony of Milton B. Grossman.)

height of the generally acceptable common fluorescent tube fixture as of 1942?

\* \* \*

The Court: Range in height, do you mean from the floor?

Mr. Miketta: No. Speaking of the fixture itself, your Honor.

The Court: The depth of the fixture?

Mr. Miketta: Yes, we can call it the depth, as opposed to the width? [410]

\* \* \*

A. I should say they vary, sir, in the one-lamp fixtures about four inches, but in two-lamp fixtures they would run from 6 to 7½ or 8 inches.

Q. Now, lets just concentrate on the two-tube fixtures as of 1942. Do you know the range in width, transverse width, of those fixtures?

A. Yes, sir. In the main I would say they are from 12 to 17½, 18 inches maximum in width.

Q. Do you know what the cut-off angle acceptable, or let's say, the common ordinarily manufactured two-tube fixtures, was as of about 1942?

A. From 27 to 30, 32 degrees.

Q. In recent years has there been any change in the cut-off requirements?

A. Yes, sir, the cut-off or shielding angle has increased as lighting sources have increased in brilliancy, fluorescent lighting sources. They are now talking as almost a standard requirement 45 degrees

(Testimony of Milton B. Grossman.)

being the required cut-off angle on specifications.

Q. That is just within the last year or two?

A. Yes, sir.

Q. In designing a fixture, would you try to [411] maintain the overall dimensions within the acceptable size range that you have previously mentioned?

\* \* \*

The Witness: Yes, I would. [412]

\* \* \*

Q. If you were attempting to design this fixture, for example, or a fixture as of 1942, what limitations would you have to meet or have to take into consideration in designing such a fixture? Perhaps you don't understand my question.

A. I do. I was just trying to think.

Q. One of the limitations is, of course, the length of tube you are going to use?

A. That's right, there would be the limitation of the length of tube, the limitation of shielding that tube, either [413] arriving at the amount of shielding analytically, if I were an engineer at that time, or—at that time I wasn't an engineer, I would have done it empirically, cut and try.

Q. How would you do it empirically?

A. Cut and try. I would have mounted a tube on some sort of housing that had a ballast in it. That, of course, would establish the depth of the housing, due to the girth of the ballast. I would have mounted sockets on the housing. As a matter

(Testimony of Milton B. Grossman.)

of fact, I think there is a bare housing here that would illustrate. Then I would mount the two tubes on it, never touch pencil or paper, and with pieces of some translucent material, glass or plastic, I would arrive at what would be an evenly illuminated side shielding that wouldn't have any glare spot running down through it. And then I would arrive at some approximation of what in the trade was acceptable in the way of shielding, form of shielding, baffles or egg crate louvers.

Q. I think, Mr. Grossman, you have a sketch there which demonstrates how you would go about in this crude way determining the overall dimensions of a fixture and of transverse shielding, have you not?      A. Yes.

Mr. Miketta: May I have these marked for identification first, your Honor? [414]

The Court: They may be marked.

The Clerk: J-1 and J-2 for identification.

\* \* \*

Q. (By Mr. Miketta): What is this central red line area, Mr. Grossman?

A. It shows the cross-hatchings in red of a trapezoidal form which approximates the cross-section of the Paramount body and reflector, the Ruby Paramount fixture body and reflector.

Q. The chassis?

A. The chassis or the body. In the trade it is called the body. Adjacent to it and approximately the distance away that a fluorescent tube is nor-



(Testimony of Milton B. Grossman.)

mally placed is shown a circle to represent the circumference of the 1½ inch T-12 fluorescent tube.

Q. Does that tube have to be spaced a certain minimum distance from the ballast box or can?

A. Yes. Not by any law, but by both design factors, experience, and also the fact that if you get it too close you have a tendency to heat too much. There isn't a chance for [416] evacuation by conduction and that nature. So we make it about a quarter of an inch normally away from the tube. Incidentally, I would like to say—

The Court: You show it at about ⅜ths there?

\* \* \*

A. A trifle over a quarter, but it is rough pencil. A little under 5/16ths. [417]

Q. By Mr. Miketta: What is this bottom line that you have drawn there?

A. The bottom line represents where a bottom surface of some form, either reflective surface or transmitting surface like glass would be put, and it also represents the bottom in case of a reflective surface, such as baffles or egg-shaped louvers of what would be the shielding unit used, whether it is a baffle as we have here, or an egg-shaped louver, type of rectangular louver, and that we use an optimum dimension of two inches.

The Court: What?

The Witness: A dimension of two inches in height for the baffle as an average. Sometimes the baffle doesn't have a rectangular shape, so we use

(Testimony of Milton B. Grossman.)

an average figure of two inches. The shape may run all the way from  $2\frac{1}{2}$  down to a half inch. [418]

A. This 6-inch dimension is a resultant dimension, not a primary one. It results from the fact that the tube is placed on this body which is housed around a ballast of a certain dimension, and then from the tube we try to get to a point or a plane that represents two inches below the bottom point of the tube that we might be wanting to shield.

Q. All right. Now, suppose that baffle is going to be two inches high, where do we go from there? How do we establish the number of those transverse baffles?

A. The numbers are resultants. We don't establish them. The numbers are definitely resultant. If we want to get a shielding that represents 30 degrees—I am looking now at another sheet.

Q. That is J-2.

A. Called J-2. If we took a triangle where the height of the baffle or the average height of the baffle, or the altitude——

Q. Is that indicated here on the left-hand side?

A. Yes, they show it here as two inches. The tangent of [419] the angle of 30 degrees is 0.557, and if that ratio is worked out, I think you will find it comes to 3.5, I will say, approximately.

Q. Mr. Grossman, couldn't you just draw that vertical representation that is 2 inches long, draw your diagonal of 30 degrees, then just scale off this distance?

(Testimony of Milton B. Grossman.)

A. Sure. But I don't do it that way. I do it mathematically.

Q. But suppose you did scale that off, how much would that come out to?

A. Approximately three and a half, 3.5.

Q. Your tube is 48 inches long, divide that by 3.5, or how many times 3.5 would give you the 48 inches or thereabouts? A. 13, 14.

Q. So you would have about 14 spaces, is that right? A. Yes.

Q. Three and a half times 14, that gives you 49 inches.

The Court: Of course that is all predicated on a 2-inch baffle?

The Witness: Yes. An average, sir, of 2 inches. In the case of this unit we struck an average, in checking it over before it went into this new data book, we struck an average of 2 inches, because the unit varies from about almost two and three-quarters in height—that is, the baffle does—down to about a half inch where it joins the frame on the side. But the height from the bottom of the tube to where we want [420] the bottom of the baffle to be was approximately two inches.

The Court: I don't think they will be of too much probative value, but I will permit their introduction. J-1 and J-2 in evidence.

Q. (By Mr. Miketta): Have you ever designed fixtures in accordance with—not in accordance with, but for the purpose of fulfilling a specification that had been submitted? A. Oh, yes, quite often.

(Testimony of Milton B. Grossman.)

Q. And those specifications do not call for any particular ornamental design, do they, Mr. Grossman?

A. Never to my knowledge have I seen a spec where an ornamental design in any way has been specified \* \* \*. But I have never seen a specific ornamentation, shape, or so forth, specified. [421]

Q. Are you familiar with the type of fixture which is illustrated in Defendant's Exhibit I-3?

A. Yes, sir.

Q. Does that illustrate any characteristics common to the fixture made by the defendant here and forming the subject of this action, and, if so, please identify those characteristics?

A. This is a classic U.R.C. type of fixture, U.R.C. being——

Q. Just point to the characteristics that are similar, and identify them.

A. Well, it covers the knock-outs on the end with a circular three-dimensional plate. It has what we have been calling step-down ends. It has sloping sides of glass, evidently, from the appearance here. It has patterned cut-outs in the end plate in order to possibly lighten the metal—I think they are cut-outs from this illustration—to lighten the metal, and, also, to let light come through the ends, so as to be transparent.

Q. Now, I call your attention to Exhibit I-7, which is the Masterson patent, and ask you if you see any characteristics or elements there that are common to the defendant's device.



(Testimony of Milton B. Grossman.)

A. Well, this—I am looking at Fig. 2, and the cross-section shows a sloping bottom, the [422] baffles off-horizontally, and it shows a V-shaped central body, which is also a V-shaped central cut-off unit, equivalent to and functions in the same way as the V-shaped longitudinal unit in the Ruby Paramount. It shows both crosswise and lengthwise louvers or baffles, and it shows side panels that are transparent. That is noted in Fig. 1 as No. 2.

Q. I call your attention to Exhibit I-11, and may I ask this question, in order to expedite it:

Is it not correct, Mr. Grossman, that this also shows a fluorescent tube fixture, with a normally open bottom, inclined upwardly and outwardly transparent sides, an end plate in Figure 5, which is of the step-down type and permits light to be discharged against the ceiling, and I believe it states that the V-shaped louver identified by the numeral 30 acts as a louver and a reflector; is that about correct?

A. Yes, sir. [423]

\* \* \*

Q. (By Mr. Miketta): Mr. Grossman, can you identify Exhibit G, for identification, items 1 to 11?

The Court: Did you make these drawings?

The Witness: They were made under my supervision, sir. I am checking.

The Court: What is No. 1—a cross-section of the Ruby louver? [424]

The Witness: Yes. It is a cross-section of a drawing made from old catalog data of these Ruby fixtures. That catalog was dated 1941.

(Testimony of Milton B. Grossman.)

Q. (By Mr. Miketta): Is that drawing approximately to scale, Mr. Grossman?

A. Yes. If I recall correctly, we did these drawings at half-scale, that is, a half inch equal to one inch.

Q. What is item 2 of Exhibit G?

A. That is a louver II, a four-light type of fixture.

Q. Made by?

A. Made by Ruby. It is dated 1941 and it shows an open-end light. It shows off-ceiling ends, and it shows sloping sides, and cut-off angles.

Q. And the data was taken from a 1941 Ruby catalog; is that correct?      A. Yes, sir.

Q. Now, item 3 of Exhibit G?

A. The item 3 is a Ruby Admiral, dated 1941, and it shows a step-down end, and it shows a sloping side, and it shows the bottom there.

Q. Item 4 of Exhibit G is what?

A. That is a fixture I was curious about. [425] When I gave a deposition to Mr. Foster, he brought out a lot of old catalogs, and one of them was one I had never heard of, the Gill Company. So I went to some effort and dug up this Gill catalog, and this is one of the fixtures I found in it, and typifies the sloping side and the dropped end.

Q. Was that in 1941?

A. Yes, sir. That was dated 1941, too.

Q. And item 5 is what?

A. This is also an old Ruby fixture, and it is a sort of grand-daddy to the present Ruby Regent,

(Testimony of Milton B. Grossman.)

with sloping sides, step-down ends and baffle bottom, and a good angle of cut-off, by the way.

Q. Does that have longitudinal and transverse baffles?

A. Yes, it has both longitudinal and transverse baffles.

Q. Now, No. 6.

A. This is a fixture entitled "Garcey-Gram Unit," dated 1941. As I recall, this is another fixture I dug up after the deposition. It shows sloping sides. It is the only fixture, by the way, in this whole group that doesn't have a step-down, but it has sloping sides and the off-horizontal bottom, and translucent side panels.

Q. And both longitudinal and transverse baffles?

A. Yes, it did.

Q. Item 7 is what?

A. That is another one of the Gill fixtures, step-down end, and [426] instead of sloping, it had angular curved sides put in at an angle off the vertical. It is dated 1941 also.

Q. The figure on tab 8 is simply a depiction of the Ruby Paramount fixture; is that correct?

A. Yes, it is.

Q. And Figure 9—

The Court: Just a moment. What do you mean on 8 when you say "greater angle than Viz-Aid," referring to the bottom?

The Witness: The angle between the horizontal and the bottom line on either side of the baffle, of the cross-wise baffle, we attempted to evaluate from

(Testimony of Milton B. Grossman.)

the samples available to us or the drawings available to us. If I recall correctly, this one was based on two pieces of louvers that we had that had been taken out temporarily of a Paramount unit, and out of a Viz-aid unit, and then we evaluated the angles. It was different.

\* \* \*

Q. (By Mr. Miketta): You are referring to tab 10 of Exhibit G. A. Yes, sir; that's right.

Q. Does that show the comparison between the transverse louvers [427] of the defendant's fixture and of the Viz-aid?

A. Yes, sir. We did this very precisely at that time. As I look at this, well,—

Q. What are the differences?

A. Well, the differences are these. There is a difference in depth between the Ruby and the Day-Brite fixture the Ruby and the Day-Brite baffle. The Day-Brite baffle is deeper in the dimension taken from some line that might be called the top line. It has a cut-out on top of the baffle to accommodate the close proximity to the tube. The Ruby one doesn't need that because it is shaped thinner. It is a two-dimensional baffle, and not only is it formed in a crosswise plane, it is two-dimensional and it is also formed on two planes perpendicularly to the cross plane, in order to accommodate the method they use of attaching their baffle to the entire frame of the unit.

The Ruby baffle is one-dimensional, one single plane unit, that is fitted into slots on the railing that



(Testimony of Milton B. Grossman.)

made up the baffle frame. The form of the "V" in the Ruby baffle, or the form of the aperture in the center of the Ruby baffle, in order to fit it around the Ruby V-shaped longitudinal louver, is a complete "V," while the form of the Day-Brite one is a truncated triangle or keystone, because the Day-Brite unit had a slot in there.

Q. That truncation you referred to is represented by [428] the horizontal solid line which appears to bisect the dotted "V" of the Paramount?

A. Yes, sir. The complete angles were different, too.

The Court: Which subdivision are you referring to now?

Mr. Miketta: That is tab 10. That is the comparison.

The Court: Tab 10 shows superimposed a solid and a dotted baffle, and the notations indicate that the solid is the Day-Brite and the dotted is the Ruby?

Mr. Miketta: That is correct. [429]

\* \* \*

Q. Mr. Grossman, you called attention to the fact that the louver assembly of the defendant's fixture is arranged differently from that of the plaintiff's Viz-aïd fixture. Does that mode of assembly also change the appearance of the fixture?

A. Quite definitely.

(Testimony of Milton B. Grossman.)

Q. In which way? Will you point it out, please? From where you stand, can you do that?

A. The Ruby fixture, since its baffles are [430] attached to a separate frame, also has a line of illumination between the side panel and the frame that houses the baffles. In other words, the whole baffle section is a completely separate unit.

\* \* \*

Q. (By Mr. Miketta): And that line of light would extend completely across the fixture?

A. Yes, sir.

The Court: That is Plaintiff's Exhibit 14 or 15 you have up there?

Mr. Miketta: That is 15, your Honor. This is the four-tube light.

The Court: Being one of the accused devices.

The Witness: As a result of that mechanical form of baffle housing, the end plate has quite a different, completely [431] different shape than the type of end plate that they use on the Viz-aid fixture. It has slots in it. It is all of one piece. It doesn't consist of a part that swings down with the baffles. It exists simply as a supporting member, to support the side panels, and it exists functionally to support the side panels on the panel housing.

Q. (By Mr. Miketta): Mr. Grossman, have you examined the plaintiff's Day-Brite fixture, as well as the defendant's Ruby fixtures?

A. Yes, I did.

Q. And you have been able to find approximately

(Testimony of Milton B. Grossman.)

18 or 19 differences between the plaintiff's fixture and the defendant's fixture?

A. I have, sir.

\* \* \*

The Court: We let the plaintiff put in his contentions of similarity as just contentions, and you may offer this as your list of contentions with the understanding that if you interrogated your witness he would say each one of those is a point of difference. [432]

\* \* \*

The Court: I want to ask a question or two here. Your cut-off point or your cut-off angle on any one of these lighting fixtures could or would vary with the height of the fixture above the work surface, would it not? For instance, supposing I have a small room and I need light at some distance from the fixture, your cut-off angle, meaning that angle of a baffle which would prevent me sitting at a work table, say, from having the globe shine in my eyes,—could be a very small angle?

The Witness: Yes, sir; except this——

The Court: On the other hand, if I had a fixture directly over my head at a work surface, probably no baffle would cut off the direct light from shining in my eyes, if I [433] looked up into it?

The Witness: If you looked up to it, sir. But that isn't how fixtures are designed or tested for their limitations. You are considered to have an optical angle of approximately 60 degrees; 30 degrees above the horizontal and 30 degrees below.

(Testimony of Milton B. Grossman.)

That was the whole consideration. That is why the cut-off, which establishes an optimum norm of 30 degrees,—

The Court: It is only a norm?

The Witness: It is a norm.

The Court: Depending on where the person would put the fixture, how far the fixture would be from the work surface, or, how far the fixture would be removed from the work surface?

The Witness: Yes, sir. But when it is stated in terms of test value, it is stated in terms of the geometric relationship between the baffle sides, the differences between them, and the length and width of the fixture.

The Court: Now, directing your attention to the side panel of glass, I am going to take, for example, Plaintiff's Exhibit 15 in evidence, one of the Ruby accused fixtures. I take it the side panel is made of glass instead of metal in order to allow light to go through it?

The Witness: Yes, sir.

The Court: If you didn't want light to go through it, [434] you would make that of solid metal?

The Witness: Yes, sir. [435]

\* \* \*

The Court: Let's contrast the side panel in the shape of the Ruby light, Exhibit 15, where the bottom portion of the panel is closer to the center of the fixture, and the top part of the panel is fur-



(Testimony of Milton B. Grossman.)

ther away, and the degree may be from the eye, oh, 60 degrees or more than 45 from the vertical plane, —is that about right?

The Witness: As in this fixture, yes, sir; approximately.

The Court: Contrast that with one where the degree of angle from the vertical plane would be almost reversed, and take you over past 90 and, say, 100 or 110 degrees from the vertical plane. The supposed panel I am talking about would supply through the panel more light to the ceiling than the panel which we have here in Exhibit 15, would it not? I am talking about the panel now.

The Witness: This panel supplies no light to the ceiling, sir. This panel—the only light this panel supplies is by reflection from the inner surface of the panel, and very little possibly from the top of the panel.

The Court: In other words, on this Ruby light the panel is designed with that angle, to reflect light downwards?

The Witness: To transmit light downwards, sir, and reflecting the light upwards.

The Court: And if you wanted it to transmit more light downwards, you would increase the angle, would you not? [436] In other words, supposing instead of being at a 60-degree angle, you would have 45 degrees. Wouldn't there ordinarily be more light transmitted downward and less to the sides?

The Witness: That would only be permissible design-wise if your tube position could be varied,

(Testimony of Milton B. Grossman.)

too. But the position of the tube controls the position of the angle of that panel. That panel is approximately at right angles to the diameter of the tube, which is in relation to the surface out of which the tube sockets come in. I might be able to show the judge with that body over there what I mean. [437]

\* \* \*

The Court: When you refer to the relation of the tube to the body you refer to taking on G-8 the position of the tube and the line running through the center of the tube at right angles to that portion of the chassis or can?

The Witness: Yes.

\* \* \*

The Court: The angle now shown as 70 degrees from a vertical plane, supposing the angle on the side panel were 45 degrees, what would be the effect on light coming from that bulb?

The Witness: You would be sending more light up to the ceiling.

The Court: By reflection?

The Witness: By reflection, and also direct transmission, if I may point out. If the angle were at, say, 30 [438] degrees off the vertical, all of this open space then would permit lights to go up, there would be additional reflection, and you would have a relatively——

The Court: What about the light that went through the panel?

The Witness: You would get a little better trans-

(Testimony of Milton B. Grossman.)

mission of light through the panel, sir, because the panel would be normal, then, to the axis, cross-sectional axis of the tube.

The Court: Isn't there involved, also, the refraction of light through glass?

The Witness: Yes. We use plastic a lot. In looking at that fixture I wouldn't be able to tell you now whether it is glass or plastic. They are approximately identical in refractive index. And that enters into it, too, sir.

The Court: By refraction you mean turning the course of a direct light ray?

The Witness: Yes, sir, slowing it down, so to speak, and swinging it off its original path.

The Court: So that by varying the slope of the panel you get various results?

The Witness: Yes, sir. In the old days, if I may enlarge on that, based on experience with incandescents, the work was done empirically on a cut and try basis, working with glass, shaping glass. The old fixture manufacturers used to have their own glass-forming departments which molded glass, [439] shaped glass and cut glass, to be able by cut, make and trim to arrive at proper things. They didn't use the analytical approach that we use today.

The Court: Counsel, are you going to offer your Exhibit G in evidence?

Mr. Miketta: If you please. May I offer that in evidence?

The Court: It will be received.

\* \* \*

(Testimony of Milton B. Grossman.)

Q. (By Mr. Miketta: Have you measured the angle from the vertical of the glass circular fixture which is in the District Court Clerk's room and all over this building?

A. I did. I measured it this morning when I came in.

Q. What is the angle of inclination of that side?

A. It is approximately 20 degrees off the vertical or 70 degrees off the horizontal.

Mr. Miketta: May the court please, I would like to have the court's authority to take a photograph of this particular fixture and introduce the photograph in evidence. I don't believe the building inspector would want me to make this a permanent exhibit. [440]

The Court: You may put a photograph in evidence and in that way preserve the building's fixture. We will assign it a number. What will it be, Mr. Clerk?

The Clerk: Defendant's Exhibit L, your [441] Honor.

\* \* \*

### Cross-Examination

By Mr. Foster:

Q. Mr. Grossman, while you were with the defendant corporation did you ever actually sell any fixtures to users of the fixtures?

A. Yes, sir, to the agents of the users.

Q. You never sold any lighting fixtures for the



(Testimony of Milton B. Grossman.)

defendant corporation directly to the ultimate users of those fixtures, did you?

A. Yes, I did. [446]

Q. On how many instances? There were very few instances, weren't there?

A. No, sir; innumerable instances.

Q. You listed at length in the record yesterday the criteria in which the purchasers of lighting fixtures like Plaintiff's Exhibits 14 and 15, the Ruby fixture, are interested when they buy lighting fixtures, such as the distribution patterns and the coefficients of utilization, angular dispersions, percentages upward or downward, absence of glare points, and so and so on. Is it necessary to take all of these various qualities or criteria into consideration in designing a fixture for fluorescent lamps which is to be commercially successful?

A. Yes, sir. Are you referring to the fixture on the stand now?

Q. Yes.

A. The two-tube and four-tube Ruby Paramount fixture?

Q. Yes. You understood that in answering my question?

A. I took it for granted that is what you meant.

Q. And from the little I understand about all of these criteria and qualities, they appear to be so technical that for one to design a commercially successful fixture, paying attention to all of them, it would require technical training such as yours in the lighting field, is that true, Mr. Grossman? [447]

(Testimony of Milton B. Grossman.)

A. No, sir, that isn't true. And it isn't true any more than it would be true if you said to Edison when he was alive, "You couldn't invent these things, you are not an engineer." But Edison did invent them by a cut and try method. [448]

\* \* \*

Q. (By Mr. Foster): At any rate, there is not much hope of commercial success for a fluorescent light fixture which does not fulfill these criteria and requirements that you enumerated yesterday, the examples of which I have given today; that is correct, isn't it?

A. No, sir. You are quite correct.

Q. Now, in order to determine all of these criteria which you mentioned yesterday, and a part of which I have given today, you mentioned also surface brightness of certain sections, the method by which the lighting is distributed, specifications as to the strength of the material, transmission qualities of certain parts, reflective qualities of other parts, and so forth, and you mentioned possibly 15 other specifications. In determining whether a fixture of a given design has all of these qualifications or qualities or criteria, I suppose you need a light meter?

A. That would be one instrument.

Q. There would be other instruments you would need in order to do a job of determining whether the fixture met those specifications and requirements; is that correct? [449]

A. It would be today, but it wasn't in the past.

(Testimony of Milton B. Grossman.)

Q. Well, what would be needed today?

A. Today a firm would have to have a distribution photometer, a brightness meter something like the Lukiesch-Taylor meter; it would have to have volt meters and ammeters. It would have to have reflectance meters—either Gross meters of direct reflectance, photometers, and some other measurement instruments of a similar nature, if they wanted to make a strict, rigid, technical evaluation of the unit to meet today's requirements.

\* \* \*

Q. When was it you went to work for Ruby, the defendant here?      A. Around July, 1947.

Q. What, of the apparatus you have just described did [450] you see there when you went to work for Ruby in the defendant's plant?

A. They had photometers.

Q. What else, that you have described?

A. They had ammeters, and I think I saw a volt-meter there. I am not sure.

Q. Is that all that you have described that you would need today, that you saw there?

A. That's all. Then measuring instruments of various types. [451]

\* \* \*

Q. But prior to your employment by Ruby in July, 1947, when the Paramount design, Plaintiff's Exhibit 14 and 15, was on the market, you had had nothing to do with the design, or had you?

A. No, sir.

(Testimony of Milton B. Grossman.)

Q. Did you make subsequently a re-design of that Paramount fixture to improve its functional design?

A. Yes, sir. I recall that we worked on the functional requirements of making the movement of the baffle easier for the maintenance man. We worked out a method of using the Ruby, exclusively Ruby spring latch deal, so that the maintenance man would not have to move the whole baffle frame laterally in order to open it up. That was one of the things. And there were some other elements of design that I recall working on. Specifically—I mean I don't recall the specific elements, but we did work on various functional maintenance elements of it. [452]

Q. When did you do this redesigning of the Paramount fixture, Plaintiff's Exhibit 14 and 15?

A. During the period that I was working on the new data book from about July to December, 1948.

\* \* \*

Q. Did you make any recommendations to the defendant corporation in December, 1948, or later, that you be authorized by the defendant to further revise the design of the Paramount fixture?

A. The only recommendation——

Q. Did you or didn't you, please, sir? Did you make such a recommendation or did you not?

A. No, I didn't, sir.

Q. Very well. In the redesigning of the Paramount fixture which you did for the defendant between July 1948 and December 1948, you did not change any of the decorations on the end cap or on



(Testimony of Milton B. Grossman.)

the medallion at the middle of the sides of the fixtures, did you?

A. I couldn't answer that question. Some redesigning of the casting was done as a result of a change in the form of the casting, and whether the patterning that resulted from that change in form is identical in this fixture to what it was prior to my being with Ruby I couldn't answer right now.

Q. What I would like you to do, and please listen carefully to this question, Mr. Grossman, is to list those differences in the appearance of the decoration upon the ends of the fixtures, Plaintiff's Exhibit 14 and 15, and the medallion in the middle of the sides of the fixtures, which you changed in revising the design in 1948, between July and December [454] to provide a more functional design.

A. I couldn't do it, sir. I have no knowledge.

Q. Did you change the overall length of the fixture in that redesign to provide a more functional design?

A. The length might have been changed because the casting, as I recall, was made a little thinner.

Q. Do you recall that you did increase or vary the length?

A. No, sir, I couldn't swear that I did.

Q. Do you recall that you changed the overall height of the fixture?           A. No, sir.

Q. Did you change the overall width of the fixture?

A. I think the width on the redesign might have been changed, because we were attempting to remove

(Testimony of Milton B. Grossman.)

the slot and it didn't require that extra eighth of an inch thickness—not thickness, but width.

Q. Do you know whether you changed the overall width of the fixture in such redesign?

A. No, I couldn't say yes or no to that.

Q. Did you change the number of transverse louvers in that fixture in that redesign?

A. No, sir, I didn't.

Q. Did you change the angle between the sides of the longitudinal V-shaped louver in that redesign? [455]

A. No, sir.

Q. Did you change the angle with the horizontal of the upper or lower edges, slanting edges, of the ends of that design?

A. No, sir.

Q. Did you change the angle with the vertical of the sides of the ends of that design?

A. No, sir.

\* \* \*

Q. There are in evidence here some catalogs containing illustrations of the Paramount fixture like Plaintiff's Exhibit 14 or 15. Did you ever see, while you were employed by the defendant corporation, any advertisements distributed by that company of its Paramount lighting fixtures other than catalog sheets illustrating them? [456]

A. There are various catalog sheets. I would like to know the one you are talking about.

Q. I am referring to catalog sheets in general that were put out to the trade by the Ruby Corporation. Do you know of any other advertisements that were distributed by the defendant of its Paramount

(Testimony of Milton B. Grossman.)

fixture besides the catalogs distributed to the trade?

A. Yes. Individual data sheets in short quantities were run off sometimes when a request was made for some illustrations of either a fixture or its use.

Q. Do you know of any advertisements that were placed in magazines or trade publications by the defendant corporation offering for sale or illustrating the Paramount fixture? A. No.

Q. And you were with the defendant corporation commencing in July 1947 until what date?

A. About August, '48.

Q. And neither before that employment——

A. One moment, please. You said 1947, didn't you, sir?

Q. That is what I understood was the date when you went to work for——

A. No, that is incorrect. I went to work for Ruby on July 17, 1948, and I terminated in August, 1949.

Q. Neither before that employment, nor during it, nor after the employment, did you see any ads in magazines or trade [457] publications by the defendant advertising for sale and illustrating its Paramount fixtures; that is true, isn't it?

A. I don't recall any ads, no, sir.

\* \* \*

Q. In your direct examination you were asked about the range of dimensions of fixtures like the Paramount fixture Plaintiff's Exhibits 14 and 15, which made those fixtures generally acceptable, and you mentioned that for a two-lamp fluorescent light

(Testimony of Milton B. Grossman.)

fixture the height or depth might vary between 6 and 8 inches. That variation in height could be in increments of an eighth of an inch all the way from 6 up to 8 inches, couldn't it?

A. No, sir, it couldn't be. To take your words and say yes or no would be incorrect. They would have to be in increments that productive equipment of Ruby Lighting permitted of. [458]

\* \* \*

The Court: Let's end this by saying that the Court will take judicial notice that whether a plant has equipment or not, it could make tools and make jigs and dies and could make equipment in any range of fractional parts of an inch from 6 inches to 8.

Mr. Foster: Thank you.

Q. You testified that the range of widths could be 12 to 18 inches and cut-off angles varied between 27 and 32 degrees, but I don't think you testified to the range of overall lengths of a fixture that would be generally acceptable for a two-lamp fluorescent fixture, accommodating a 48-inch tube. What would be that variation?

A. It would run from 48 inches in the open type of pan fixture without any kind of surrounding element, all the way up to 51 inches, depending on the kind of end plates or assemblies, and also depending on the revisions being met, [459] such as those of the Underwriter Laboratory, which very specifically restrict dimensionally the spatial positions of knock-out, conduit holes, socket holders, and things of that



(Testimony of Milton B. Grossman.)

nature. For your information, I have a copy here of the Underwriter Laboratory Standard for Electric Lighting Fixtures, which indicates some of those restrictions which would control.

Q. Without reading that, would you attempt to answer my question, what range of overall dimensions would be generally acceptable for a two-lamp fluorescent tube fixture to accommodate a 48-inch tube?

A. Well, from 48 inches I would say up to a maximum of 54 inches. [460]

\* \* \*

Q. Are all of the designs which you have shown in Defendant's Exhibit G functional designs?

A. Yes. I think they are pretty good.

Q. You used that term "functional design" several times in your direct examination. What is your definition of it, as you have used it?

A. My understanding of a functional design, as far as a product is concerned, a house, or anything of utilitarian purpose, is a design whose form overall originates from the essential functions of the product; a design that aesthetically is good, because functionally—because it follows in its design elements the functional requisites and purposes of the item.

Q. You are a disciple of the Sullivan school, aren't you? [462]

A. To a point, yes, sir.

Q. As I understand it, the creed of that school

(Testimony of Milton B. Grossman.)

may be briefly stated as being that function determines form?

The Court: What school is this?

The Witness: Sullivan and Frank Lloyd Wright.

Q. (By Mr. Foster): Is that correct?

A. It is a vulgarization of it, but it amounts to that.

Q. I direct your attention to Defendant's Exhibit I, and particularly, the patents which are contained in that exhibit, being tabs 1 to 16, and showing light fixtures. You have looked over that exhibit?

A. In a cursory way, I have.

Q. Are the fixtures which are shown in those tabs, 1 to 16 of that exhibit, of functional design?

A. Categorically, or can I indicate my reaction to the individual ones?

Q. Can you, from your knowledge in having looked through them, indicate whether they are, in general, functional designs?

Mr. Miketta: Mr. Foster, I understand you were just asking a general question. You do not want a detailed analysis?

Mr. Foster: No. That is what I am asking.

The Witness: If it is a general question, I will answer [463] it with a general answer, that some of these, in the main, have good functional design, but they are overloaded with a lot of trim which in their day was considered necessary but which today isn't.

Q. (By Mr. Foster): But as to their over-all

(Testimony of Milton B. Grossman.)

appearance in general the fixtures shown in 1 to 16 of defendant's Exhibit I are, in general, of functional design?

A. Some of them are. I take exception to calling No. 5 anything functional in its over-all entity, although it has elements of functional design in terms of the proper use of the light output, but the rococo effect that has been tied into it is not functional.

Q. The same is true, isn't it, as regards the lighting fixtures shown in the catalogs 17 to 20, included in Defendant's Exhibit I, that is, having regard to their over-all appearance?

A. First of all, if I may correct you, sir, they are not catalogs. They are excerpts from Illuminating Engineering, dated February, 1941.

Q. With that correction, will you direct your attention to that, and isn't it true the fixtures there shown, with regard to their over-all appearance, generally are of a functional design?

A. In the main, they are.

\* \* \*

Q. Did you mean, when you used the term "functional design," that you had reference to the over-all appearance of the fixture?

A. No, I mean the end aesthetic result. [465]

Q. Of the fixture?

A. Of the fixture. [466]

\* \* \*

Q. (By Mr. Foster): During the time you were employed by the defendant corporation, how many

(Testimony of Milton B. Grossman.)

salesmen did it have—how many employees who were devoting efforts to sales of the Paramount fixture?

A. I don't know that anyone was ever devoting any effort to the sale of the Paramount fixture. It was considered a very bad fixture.

Q. What efforts, to your knowledge, did the corporation make to sell those fixtures, either before you were employed by that company, or during such employ?

A. None that I know of, other than to include it in the catalog I worked on with the other fixtures that were included, which were no longer being produced. [467]

\* \* \*

Mr. Miketta: Now, at this time I make this offer of proof, that Mr. Ruby, if called upon to testify, would testify that the fixtures whose outlines are indicated on Exhibit G, tab 1, tab 2, and tab 3, were made, manufactured and sold in appreciable quantities during the year 1941 and for several years thereafter, but are not being sold at the present time because fixtures closely resembling those fixtures were copied by the Sunbeam crowd, their former employees, so they had to change their designs in order to try to distinguish [469] from the Sunbeam fixtures which were being manufactured.

The Court: Will you so stipulate, Mr. Foster?

Mr. Foster: I will so stipulate, that he would, if called to testify, so testify.

\* \* \*



The Court: The witness' name that this stipulation concerns is Mr. Ruby?

Mr. Miketta: Yes, Mr. Benjamin Ruby. [470]

\* \* \*

The Court: Let's modify the stipulation. That he would testify that the fixtures diagramed on tab 1, 2 and 3 were made by him and sold in appreciable quantities in 1941 and for several years later, but are not being sold now?

Mr. Foster: I will so stipulate.

Mr. Miketta: Very well. [471]

\* \* \*

Mr. Foster: We rest, with this exception: I would like to repeat the request—I would have asked Mr. Ruby had he gone on the stand—that the record show the number of sales of the Ruby Paramount fixture by the month from the beginning until date, approximately, and I am perfectly willing to stipulate that may be filed when it is compiled, if it takes any compiling, and it be deemed that Mr. Ruby has testified to the approximate correctness of the figure.

Mr. Miketta: I believe that should be held in abeyance until your Honor has decided the prime issue.

The Court: You want it on the issue of whether there was a substantial or a nominal amount of sales?

Mr. Foster: Yes, I want it on that and would argue from that that this shows an appropriation of

our market that we had created at substantial expense. [472]

The Court: I think it would be proper to inquire what those sales amounted to without being proof on the issue of damages, but on the general subject, Was there only one of two fixtures sold or Were there a million of them sold? In other words, are we dealing with a matter that is of trifles, or are we dealing with something that is substantial?

It need only be an approximation. It may be enlarged upon and made more certain if necessary, if there is hereafter any further proceedings on the matter of damages.

Mr. Miketta: Will the court accept my statement as to the figure?

Mr. Foster: I will accept it.

The Court: Yes.

Mr. Miketta: I will just give the hundred figures, your Honor. For the year 1947——

The Court: What fixture are you talking about?

Mr. Miketta: We are talking about the defendant's two-tube Paramount fixture.

The Court: All right.

Mr. Miketta: Illustrated by Plaintiff's Exhibit 14.

For the year 1947 the sales amounted to a little over 600.

The Court: Dollars or units?

Mr. Miketta: Fixtures.

For the year 1948, a little over 1300 fixtures. [473]

For the year 1949, a little over 500 fixtures.

Mr. Foster: Where there sales of the four-tube, too?

Mr. Miketta: No.

The Court: You say you don't have it on the four-tube?

Mr. Miketta: No, your Honor. There is this to be remembered——

Mr. Foster: You don't have figures or there weren't any sold?

Mr. Miketta: I do not have any figures for that.

\* \* \*

Mr. Miketta: Frankly, this is something that your Honor should consider: The plaintiff's fixture is a two-tube fixture, they do not manufacture a four-tube fixture for this design and therefore there is no competition. [474]

\* \* \*

The Court: ——I am wondering if we should not dispose of your motion to file this third cause of action by amendment, before we get into the argument, for the bearing it will have on the argument. [483]

\* \* \*

I think I would like to hear from Mr. Miketta as to whether he will be hurt in any way by the filing of the amendment.

Mr. Miketta: Very frankly, your Honor, this court has authority under Rule 15(b) to accept such an amendment. That particular cause of action will either stand or fall on the evidence, and I am willing to have your Honor admit it, and I will not press

any further objection to it, as, under the law, I think it is permissible.

The Court: Your defense to it would be the same type of defense you made to the other causes of action, would it not?

Mr. Miketta: It either stands or falls on the evidence as it is.

The Court: All right. I am, therefore, going to grant the motion to file the document entitled "First Amendment to the Complaint," lodged March 2, 1950. It will be filed [484] by the clerk.

Now, in order to have the issues under that cause of action, what can we do?

Mr. Miketta: May I just orally deny the allegations of that amended complaint or that amendment to the complaint?

Mr. Foster: That is acceptable to the plaintiff, your Honor. I presume that a formal written answer should be filed, and we are agreeable to its being filed at any convenient time by the defendant, and to be taken as filed now.

Mr. Miketta: Very well.

The Court: All right. I take it there will probably be no objection to Paragraphs 1 and 2 on the question of jurisdiction?

Mr. Miketta: No, your Honor.

The Court: The defendant then denies orally each and every allegation of Paragraphs 3 and 4?

Mr. Miketta: Yes, your Honor.

The Court: And permission is granted to the defendant to subsequently file a formal written answer, to be filed in the records of this court.



Mr. Miketta: Very well, your Honor. It shall be done.

The Court: To be filed within five days. Is five days sufficient?

Mr. Miketta: Oh, yes; surely. [485]

The Court: All right. [486]

\* \* \*

The Court: I could understand those cases if they referred [509] to the design in toto. But do you contend that those cases go so far as to hold that if there was one part of this design which had a mechanical function or a functional purpose, and someone else prepared a design where they used that particular portion that was in there for a functional purpose, that they would infringe on the first patent?

Mr. Foster: No, sir, I do not. I think the separate parts of any patented design which have mechanical utility, they are free for use by anyone. But I think this statement more nearly applies to the facts here: That the patented design is a composite whole or summation of a number of elements of appearance. Some of those elements of appearance are related to parts that have utility and they must have somewhat the same design, shape or configuration, perhaps, or relation to the other parts that they do have that utility. For example, the angle of the sides here is one that permits the sides of the shield to have utility. The angle could be a different angle according to the testimony than the angle it is, within rather a wide range, and still the entire fixture would have utility. So that no design

patent can prevent a rival manufacturer from making a fixture in which the sides are at an angle to the vertical or the horizontal. But I say, and I think the decisions support the declaration, that the design patent on such a device as this fixture covers the composite whole, the overall general appearance to the eye, [510] and a part of that is the angle of the sides of the fixture in relation to the other parts of the fixture, and that we must look always at the composite whole. And the fact that those elements, their relation or shape or their special relation to the other parts contributes to the utility of the design, as for example that the angle of the sides permits light to be transmitted, and that is useful, does not detract from the patent-ability. Those relationships, those shapes, could be changed, their relationship to each other could be changed greatly and we would still have a useful lamp.

We don't seek to prevent anyone from doing that. I think that is borne out by the testimony of the last witness who is a disciple of the Sullivan school of form that utility or function dictates the form. He found that there were functional designs in practically all of these prior lamps in the catalogs, and yet to me their overall appearance and appeal are very different from each other, and yet they have function.

I divorce in my own mind, and I think it is proper, your Honor, the definition of functionality as applied to the element into two concepts: One, where the element has no function unless it has a particular shape with relation to the other parts that it has, and the other where the element has some func-

tion in that shape compared to the other dimension and with relation to the other parts, but would also have a function of a different shape, different relative dimensions and different [511] relationship to the parts. And it is to the latter, your Honor, that I direct the statement and these decisions that the functionality or the fact that the patented design has utility, functions well for an intended purpose, does not detract from its patentability. [512]

\* \* \*

Mr. Miketta: While your Honor's mind is still on the matter of the secondary meaning. I will agree with counsel for the plaintiff in this, that, under the proper conditions, a person can acquire a secondary meaning in the dress of an article.

The Court: Without a name?

Mr. Miketta: Yes, irrespective of name, your Honor. That is very true.

The Court: You mean, for instance, a package?

Mr. Miketta: That is right.

The Court: Suppose I put out a package with red, white, and blue stripes around it for years and spent money on it, you mean that package dress might become so well identified with my name that you wouldn't think of the red, white, and blue stripes, but think of the article inside of it?

Mr. Miketta: And, very important, think of the manufacturer. [526]

The Court: Think of the manufacturer.

Mr. Miketta: —because that is an essential part of establishing secondary meaning. [527]

\* \* \*

Mr. Miketta: In the first place, it wasn't 12 hours. Mr. Ruby, in his deposition back in May, on May 4, 1949,—if he said anything about 12 hours, I think it was in response to a leading question, because Mr. Ruby didn't want to argue. He stated that they were making the design over, say, a couple of weeks. According to his answer, he admitted he didn't work continuously on it during those couple of weeks but upon being pressed by counsel for the plaintiff, in answer to the following question, this is what happened:

“Q. Mr. Ruby, how much time continuously?

“A. A week or 10 days.

“A 35-hour week would make it 35 to 50 [549] hours:

“A. Yes, that's it.”

Now, that is the best they could get as to the amount of time that Mr. Ruby spent on it. He admitted in his deposition that he and this draftsman——

\* \* \*

The Court: Is there any objection to putting it in the record?

\* \* \*

Mr. Foster: I will stipulate he has testified to what you read from the deposition. [550]

\* \* \*

The Court: The portion read by counsel will be admitted as a part of the case. The case is reopened for that admission, and then reclosed. [551]

\* \* \*

The Court: That is right. I was reading the last



sentence. And I think I can say parenthetically here there is no direct evidence.

Mr. Foster: None direct.

The Court: That any customer in the trade associates the plaintiff's name with this type of fixture.

Mr. Foster: I think that is true. [565]

\* \* \*

As to the patent which is shown in Exhibit 3, being the patent with the smaller number, if I were to hold that patent valid as a design patent in any way that would affect the rights [571] of this defendant, I would have to take into account the side wall, the louvers, I would have to take into account the general design of that patent.

I don't think I can do that.

I have in mind this Challenger model appearing in Exhibit 9, subdivision H, which has side walls, has louvers underneath, has the same general appearance and, as a matter of fact, it was cited as a reference before the Patent Office.

If Patent 138,990 is valid, as a design patent, in my opinion it is limited to the configurations on the end. And there are no configurations on defendant's devices which are, to my mind, similar enough to constitute infringement. I therefore would not find infringement, either.

Of course, infringement wouldn't be involved if the patent weren't valid. I am assuming for argument that that part of the patent 138,990 would be valid, namely, the configurations. I don't find that the configurations on defendant's devices infringe.

The only possibility is the general outline shape

of the lamp. The outline shape is not new. The bevel bottom or the bottom being on a different line than a horizontal, the slant sides at about that angle, appear in many of these devices. The length of the device is largely controlled by the length of the bulb. At any rate, my conclusion is that [572] patent 138,990 is a valid design patent only insofar as the design and configuration on the end thereof is concerned; and that, secondly the defendant does not infringe by his design.

I reach the same conclusion as to Patent No. 2, limited, of course, to the scope of the second patent, namely, it involved the longitudinal louver. The longitudinal louver was shown in prior art, which was not considered by the Patent Office.

I seriously question whether anyone applying the test you contend for with respect to a casual observer of the device would even notice the longitudinal louver. But assume it would be noticed by a casual observer, the V-shape was shown in prior art which is in evidence.

The bead may have been new. I think you have a patent in No. 143,631. It is limited to the bead, which I don't think is shown in the device.

As to unfair competition, I have this to say, and this isn't a finding. I may make such findings as I choose, but I am just telling you what I think about this unfair competition count, because that is being taken under submission. It is hard for me to believe that Mr. Ruby even in eight or 10 hours or 12

hours working with an employee whose first name only he knew, whose last name he couldn't remember or find, could sit down and draw or have drawn for him a design as near [573] to the plaintiff's design as this one shown by Plaintiff's Exhibits 14 and 15. There is a lot of identity in those exhibits. But even if I should make that kind of finding, I am convinced that the law is, as far as the structural device alone is concerned, where there is no trademark or patent protection, that the world is free to make that device. It may be that Mr. Ruby sat down with that device in front of him and copied it or had this employee copy it. Still there is a question in my mind whether or not a cause of action of unfair competition can be stated in view of the authorities I have been looking at, and the citations I have given you.

There is not complete identity. It is not a Chinese copy. There are differences in structure, in the functional operation. There is, of course, a different design on the end. The similarity consists largely in length and height, and the number of louvers, and somewhat in the end shape, although there has been a variation in the end shape as is conceded by the exhibits here.

The evidence shows that Mr. Ruby, although he may have copied Plaintiff's Exhibit 13, or plaintiff's design patents, there is no evidence that he ever sold them as the products of the Day-Brite Company, or advertised them as the products of Day-Brite, or traded on the Day-Brite name. In the absence of some fact which would show this

misrepresentation, or some facts which would show some secondary meaning attached to [574] plaintiff's products, I cannot see a cause of action for unfair competition. I think, probably, other elements of your case are there.

You have shown the building of a market; you have shown competition.

The case will be submitted. I think from what I have said it will be submitted solely upon the ground of whether or not the authorities show a cause of action on unfair competition.

\* \* \*

As you will observe from my remarks, from the standpoint of the equities here, I would say that they rest in favor of the plaintiff. But that does not mean that the plaintiff is [575] entitled to a judgment in this cause. I am inclined to think that Mr. Ruby might be subject to some criticism, if there is any legal right that he has violated. But if I read these cases correctly, he could have sat down at a table and taken the plaintiff's device and put it in front of him and copied it verbatim and probably made a Chinese copy, and as long as he didn't say this is a Day-Brite product and not a Ruby product, there would be no legal right against him.

The case will be submitted, and thank you for your assistance and help. [576]

\* \* \*



## Certificate

I hereby certify that I am a duly appointed, qualified and acting official court reporter of the United States District Court for the Southern District of California.

I further certify that the foregoing is a true and correct transcript of the proceedings had in the above-entitled cause on the date or dates specified therein, and that said transcript is a true and correct transcription of my stenographic notes.

Dated at Los Angeles, California, this 3rd day of March, A.D. 1950.

/s/ SAMUEL GOLDSTEIN,

/s/ MARIE G. ZELLNER,  
Official Reporter.

[Endorsed]: Filed July 25, 1950.

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[Title of District Court and Cause.]

## CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the United States District Court for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 64, inclusive, contain the original Complaint; Answer to Complaint; Stipulation re Proof; First Amendment to Complaint; Answer to First Amendment to Complaint; Affidavit of C. A. Miketta re Attorneys' Fees and Costs; Findings of Fact and Conclusions of Law; Judgment and

Decree; Notice of Appeal; Cost and Supersedeas Bond on Appeal; Order Staying Judgment for Attorneys' Fees and Taxed Costs; Stipulation and Order Extending Time to Docket Appeal; Statement of Points on Appeal; Designation of Record on Appeal and Counter-Designation of Record on Appeal, and full, true and correct copy of minute order entered Mar. 22, 1950, which, together with original Plaintiff's Exhibits Nos. 1 to 20, inclusive, and original Defendant's Exhibits A to L, inclusive, and copy of reporter's transcript of proceedings on February 28, 1950, March 1, 2 and 3, 1950, (in four volumes) transmitted herewith, constitute the transcript of record on appeal to the United States Court of Appeals for the Ninth Circuit.

I further certify that my fees for preparing and certifying the foregoing record amount to \$2.00 which sum has been paid to me by appellant.

Witness my hand and the seal of said District Court this 1st day of August, A.D. 1950.

EDMUND L. SMITH,  
Clerk.

[Seal] By /s/ THEODORE HOCKE,  
Chief Deputy.

[Endorsed]: No. 12633. United States Court of Appeals for the Ninth Circuit. Day-Brite Lighting, Inc., a corporation, Appellant, vs. Ruby Lighting Corporation, Appellee. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed August 3, 1950.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for  
the Ninth Circuit.

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In the United States Court of Appeals  
for the Ninth Circuit

No. 12,633

DAY-BRITE LIGHTING, INC., a Corporation,  
Appellant,

vs.

RUBY LIGHTING CORPORATION, a Corpora-  
tion,

Appellee.

NOTICE OF ADOPTION OF  
STATEMENT OF POINTS

Appellant in the above-entitled cause hereby formally adopts as its statement of points on appeal under Rule 19(6) the Concise Statement of Plaintiff-Appellant's Points on Appeal Pursuant to F.R.C.P. 75(d), dated June 29, 1950, appearing in the record on appeal on file herein.

Dated: At Los Angeles, California, this 15th day  
of August, 1950.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.

HARRIS, KIECH, FOSTER &  
HARRIS,

WARD D. FOSTER,

JACK BARRY, JR.,

By /s/ WARD D. FOSTER,  
Attorneys for Appellant.

Receipt of Copy Acknowledged.

[Endorsed]: Filed August 21, 1950.



[Title of Court of Appeals and Cause.]

STIPULATION RE BOOKS OF EXHIBITS  
AND PRINTING OF RECORD

It Is Hereby Stipulated, by and between the parties to the above-entitled appeal, through their respective counsel and subject to the approval of the Court:

That only the following exhibit shall be included in the printed record on appeal: Plaintiff's Exhibit 17;

That the following exhibits shall not be printed in the record or included in the book of exhibits, they being physical exhibits:

Plaintiff's Exhibits 1, 2, 6 to 10, inclusive,  
13 to 16, inclusive, and 18 to 20, inclusive,  
Defendant's Exhibits A, D, E, F, and H.

That only the following exhibits shall be prepared in books of exhibits, and the Clerk is requested to prepare only six (6) copies of such books of exhibits and, when they are completed, to transmit one to counsel for each of the parties to this appeal and to retain four (4) copies for the use of the Court, and to utilize those printed copies of patents provided by counsel for either party in the preparation of said books of exhibits:

Plaintiff's Exhibits 3, 4, 5, and 11,  
Defendant's Exhibits G, I, K, and L.

Dated: At Los Angeles, California, this 17th day  
of August, 1950.

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY.

HARRIS, KIECH, FOSTER  
& HARRIS,

WARD D. FOSTER,

JACK BARRY, JR.,

By /s/ WARD D. FOSTER,  
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C. A. MIKETTA,  
WILLIAM W. GLENNY,

By /s/ C. A. MIKETTA,  
Attorneys for Appellee.

Approved and It Is So Ordered, this 21st day of  
August, 1950.

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ CLIFTON MATHEWS,

/s/ WM. E. ORR,  
Circuit Judges

[Endorsed]: Filed August 22, 1950.



No. 12633

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

DAY-BRITE LIGHTING, INC., a corporation,

*Appellant,*

*vs.*

RUBY LIGHTING CORPORATION, a corporation,

*Appellee.*

---

## BRIEF FOR APPELLEE.

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FILED





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No. 12633

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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DAY-BRITE LIGHTING, INC., a corporation,

*Appellant,*

*vs.*

RUBY LIGHTING CORPORATION, a corporation,

*Appellee.*

---

## BRIEF FOR APPELLEE.

---

### INTRODUCTION.

Appellant, Day-Brite Lighting, Inc. (plaintiff below), has appealed from a judgment rendered by the United States District Court for the Southern District of California, holding appellee, Ruby Lighting Corporation (defendant below) not guilty of infringement of two patents for design on fluorescent lighting fixtures and not guilty of a belated charge of unfair competition.

It is submitted that the judgment of the District Court must be sustained on the facts and on the applicable law and authorities. The matter is simple and clear-cut and defendant presents a short brief which sticks to the facts and the law, without oratory, in the hope that such factual presentation will assist this Court in the review of the case and the affirmation of the judgment.

---

NOTE: The parties shall be referred to as plaintiff and defendant. The references to the printed record, including Vol. II of Exhibits, shall be by R. followed by page number. Emphasized matter in decisions is by defendant.

## BRIEF STATEMENT OF THE CASE.

Appellant, plaintiff below, a Missouri corporation, manufactures about one-quarter of all of the fluorescent lighting fixtures in the United States [R. 160] and among others, owns design patents No. D138,990 and No. D143,641 [Plaintiff's Exhibits 3 and 4] here in suit and a mechanical patent No. 2,411,952 [Plaintiff's Exhibit 5, R. 348] which describes the construction used in plaintiff's fluorescent fixture sold under the name "VIZ-AID" [Plaintiff's Exhibit 15].

Defendant is a California corporation and its president and principal stockholder, Ben Ruby, started working in the lighting fixture industry in 1915 [R. 221] and organized his first lighting fixture business in 1925 [R. 222]. Mr. Ruby is thoroughly familiar with manufacturing procedures and the desires of the trade with respect to lighting fixtures. Defendant's accused fixture is sold under the name "PARAMOUNT" [Exhibits 14 and 15]. Defendant's fixture employs a different construction than that used by plaintiff.

Defendant was originally charged with infringement of the mechanical construction patent No. 2,411,952 and the two design patents [Finding of Fact 2, R. 25, 95, 105]. Later, plaintiff filed its complaint charging defendant with infringement of the two design patents only. One year and nine months later, during trial, and at the conclusion of plaintiff's case, plaintiff filed a "First Amendment to Complaint" [R. 16] charging defendant with unfair competition. Defendant admits jurisdiction. Defendant denies infringement and any acts of unfair competition. Defendant, in its answer, denied validity, but the District Court did not decide this issue.

Both plaintiff's and defendant's lighting fixtures are designed to receive and use fluorescent tubes not invented by plaintiff [R. 54]. The fixtures are commercial fixtures built to receive standard, forty-eight-inch fluorescent tubes and as a result, the overall length of the fixture is a little more than forty-eight inches [R. 92]. Plaintiff's and defendant's fixtures follow the teachings of the prior art and use louvered bottoms to prevent glare, inclined translucent side panels, and metal ends with step-downs to permit light to be cast toward the ceiling. These fixtures are sold to Federal, State, County and City purchasing officials and their engineers, and to architects and wholesale jobbers [R. 238], generally on bids which specify performance characteristics but not ornamentation [R. 185, 224-225, 241, 242]. These are commercial fixtures and are not sold to individual householders.

Design patents are limited by statute to the protection of ornamentation and cannot cover functional elements, nor those shapes and forms which are common to a class of devices.

The Court properly found that the two design patents are of limited scope [Judgment, items 2 and 3, R. 32] and the Findings of Fact clearly point out that the design patents must be limited in view of the prior art [Findings 3, 4, 5, 6, and 7, R. 26-28]. Although doubt was expressed by the Trial Court as to the validity of the two design patents, the Court did not hold them invalid, because the matter was disposed of by the holding of non-infringement.

The Court properly found that the patents were not infringed [Judgment, item 4, R. 33] and Findings of Fact 10, 11 and 14 compel the conclusion of non-infringement. Plaintiff does not attack these findings.



The Trial Court also properly found that defendant was not guilty of unfair competition [Judgment, item 5, R. 33], and Findings 12, 13 and 14 clearly require such holding. This defendant has the right to make lighting fixtures, using prior art shapes and those forms which are necessary for proper light distribution.

The Trial Court, having observed the witnesses and exhibits, and being familiar with the manner in which the case was conducted during full trial, awarded costs and attorneys' fees to defendant. This was not an abuse of discretion.

### SUMMARY OF DEFENDANT'S ARGUMENT.

It is submitted that no grounds exist upon which the judgment of the Trial Court can be justifiably reversed.

1. **Design patents must be limited to ornamentation;** the enabling statute (35 U. S. C. 73; R. S. 4929; 53 Stat. 1212) distinguishes design patents from mechanical patents (authorized by 35 U. S. C. 31) by limiting design patents to those which are directed to a "new, original and ornamental design," leaving out of the statute the words of utility and usefulness which characterize mechanical patents.
2. Design patents do not and cannot cover functional or utilitarian features for the basic reasons stated above.
3. The prior art in this case (not considered by the Patent Office in granting the design patents) and the file history limitations necessitate the imposition of but very narrow scope to the design patents in suit. **If not so limited, the design patents are invalid.**

4. Defendant does not use the ornamentation shown in the patents and does not infringe. Defendant's fixtures are functional and follow the teachings of the prior art [Finding 6, R. 27].
5. Plaintiff does not use, in its own VIZ-AID fixture, the ornamental elements of the design patents in suit. Plaintiff uses a mechanical construction which is covered by patent No. 2,411,952 not in suit. The so-called "commercial success" of plaintiff's VIZ-AID fixture is not attributable to the design patents.
6. Plaintiff has not shown that there is any secondary meaning to the form of its fixtures or that the public recognizes such form as indicating origin with plaintiff. There is **no evidence** of confusion and **no evidence** of palming off. There is no unfair competition.
7. The Trial Court, in the exercise of its discretion, properly awarded costs and attorneys' fees to defendant, because of the unjustified charges made by plaintiff and the belated charge of unfair competition, referred to in Finding of Fact 2 [R. 25-26].

PLAINTIFF DOES NOT CONTEND THAT THE FINDINGS OF FACT ARE IN ERROR. The facts compel the judgment reached by the Trial Court.

"Nowhere in appellant's brief is there a contention that the District Court's findings are erroneous; instead the argument is directed to the Trial Court's failure to find that the enumerated concepts constituted invention."

*R. G. Le Tourneau Inc. v. Garwood Industries*,  
(C. C. A. 9), 151 F. 2d 432.

## FIXTURES ARE DESIGNED FOR LIGHTING EFFICIENCY.

In the old days of candle light and gaslight, the fixture consisted of a shield to protect the candle flame from the wind. With the advent of incandescent light globes, fixtures were devised to properly distribute the light in all directions and translucent materials were used to prevent the glare of the intense light source. About twenty-five or thirty years ago the illumination engineers established the **functional shape** of a fixture for most effective light distribution, and your Honors probably have had such fixtures in your homes for at least twenty years. This fixture is shown in Defendant's Exhibit L, last page of the book of exhibits here [R. 475].

Plate I compares the profile of this old fixture with the profile of defendant's fixture and identifies the functions of the sides, bottom and upstanding portion. The profile or contour imparts efficiency in distribution of light to the fixture.

The commercial fluorescent fixtures made by plaintiff and defendant are sold on the basis of efficiency.

"Q. In selling fluorescent lighting fixtures, what do you find to be the important criterion or criteria which your purchasers seem to be interested in?

The Witness: If I had to phrase it in one word, I would say illumination efficiency" [R. 238].

Plaintiff's advertising [Exhibits 7 and 8] stresses "functionally designed" and "optically engineered." A great many prior art lighting fixtures employ the same functional arrangements as those shown in Defendant's Exhibit L. See, for example, R. 385, 389, 397, 399, 405, 412, 417, 424, 443, 444, 447, 452, 456, 460, 469, 470, 471.

Profi  
Prior  
Exhi

Profile of  
Defendant's  
Fixture



P  
P  
E

Profile of  
Plaintiff's  
Fixture







PLATE I.

Profile of  
Prior Art Fixture  
Exhibit L [R. 475]

Profile of  
Defendant's  
Fixture

Upstanding Portion  
Functions to Space

Fixture From  
Ceiling and  
Permits Light to  
Illuminate Ceiling

Inclined Sides  
Function to  
Direct Light  
Angularly to  
Side

Inclined Bottom  
Functions to  
Diffuse Light  
Downwardly

Profile of  
Prior Art Fixture  
Exhibit L [R. 475]

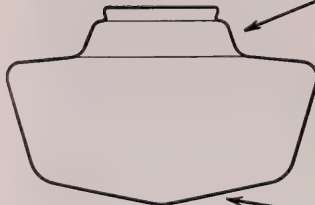
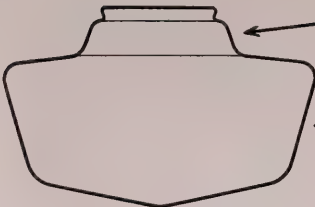
Profile of  
Plaintiff's  
Fixture

Upstanding Portion  
Functions to Space

Fixture From  
Ceiling and  
Permits Light to  
Illuminate Ceiling

Inclined Sides  
Function to  
Direct Light  
Angularly to  
Side

Inclined Bottom  
Functions to  
Diffuse Light  
Downwardly





In these lighting fixtures the *purpose* of the inclined side panels made of translucent material is to emit light angularly downwardly, and to the side [Kaepfel, R. 99; Grossman, R. 248-249]. The transverse and longitudinal louvers in the bottom are for the *purpose* of shielding the lamp from the eye of the viewer [Kaepfel, R. 99] and are common in the prior art [R. 247]. The step-down end permits the light to be thrown up on the ceiling [R. 103] and the prior art publications clearly state that this prevents objectionable ceiling contrasts [R. 245-246].

Mr. Grossman, an electrical engineer in the illumination field, who has had extensive experience in working on department store illumination, assisting buyers in the selection of equipment, etc., reviewed the prior art and pointed out that the literature taught the *purpose and function* of all these elements. For example, Defendant's Exhibit I-21 entitled "A Review of Fluorescent Luminaire Design," printed in 1940, on page 6 [R. 452], shows a design having a step-down end, a V-shaped louver and transverse louvers, and states

"A. \* \* \* 'The plastic sides and central member furnish shielding for crosswise view. The louvers shield for lengthwise view. The design of the upper part of the reflector is such as to direct light to the ceiling, thus eliminating objectionable ceiling contrasts'" [R. 245].

Mr. Grossman explained "ceiling contrasts" as follows:

"A. If the fixture is mounted as, for example, is the one in the court room, and were to be lit up and had a sharp contrasting differentiation between the brightness of the fixture itself and the ceiling, it would tend to become an object of glare to the eyes of a person that was in the room and using that fixture" [R. 245].



The step-down end is “a requirement in fixtures of this nature” [R. 246], since without it one would not get acceptable distribution of light [R. 247]. The fixture illustrated in the lower right portion on page 14 of Exhibit I-21 [R. 460] is substantially identical to defendant’s fixture [R. 249].

The length of the fixture must be sufficient to accommodate a forty-eight inch fluorescent lamp tube [R. 92] but should not be much longer, because then uniform lighting is not obtained [R. 127, 247], particularly when these fixtures are placed in end-to-end relation.

Even the cut-out end ornamentation in defendant’s fixture is partly functional in that it allows some light to be thrown beyond the end of the fixture [R. 250].

The evidence establishes that the angularity of the sides, the step-down end and the baffled bottom are **functional elements necessary to distribute light**. These elements are old in the art.

A design patent on a fixture cannot cover these functional and utilitarian features any more than a design patent on a spoon could cover the combination of a handle with a bowl portion at one end; such patent could only cover the *ornamentation* applied to the handle.

“\* \* \* Infringement therefore must lie in the details of the design rather than in the general contour, just as infringement of a design for a spoon would lie in the particular design rather than in the general contour of a spoon.”

*Lightolier Company v. Artistic Brass & Bronze Works, Inc., et al.*, 15 Fed. Supp. 323 at 324, affirmed 84 F. 2d 1007.

“The Acts of Congress, which authorize the grant of patents for designs were plainly intended to give

encouragement to *decorative arts*. They contemplate not so much utility as appearance, and that, not as an abstract impression or picture, but an aspect given to those objects mentioned in the Acts.”

*Gorham Mfg. Co. v. White*, 14 Wall. (81 U. S.) 511, 524, 20 L. Ed. 731.

“Patents for designs are intended to apply to matters of *ornament*, in which the utility depends upon the pleasing effect imparted to the eye, and not upon any new function \* \* \*. Design patents refer to appearances, not utility. Their object is to encourage works of art and decoration which appeal to the eye, to the aesthetic emotions, to the beautiful.”

*Rowe v. Blodgett & Clapp Co.*, 112 Fed. 61.

## IT IS FUNDAMENTAL THAT DESIGN PATENTS MUST BE LIMITED TO ORNAMENTATION AND CANNOT COVER FUNCTIONAL FEATURES.

Plate I clearly shows that the end view or profile of plaintiff's design patents (as indicated by the outlines of Figs. 2 of the patents) are substantially identical to the profile of the old fixture, Exhibit L [R. 475]. This same profile is shown in numerous prior fixtures illustrated in defendant's Exhibit I. This contour or profile is functional and cannot be the subject matter of a design patent, because design patents are limited to ornamentation.

This Court has correctly stated:

“\* \* \* so that the attempt to patent a mechanical function under cover of a design patent would lead to a perversion of the purposes of the statute.”

*Majestic Electric Development Co. v. Westinghouse Electric & Mfg. Co.*, 267 Fed. 676 at 678 (C. C. A. 9).

“A design patent cannot be used to monopolize functional features which cannot be protected by a mechanical patent. *Baker v. Hughes-Evans Co.*, 270 Fed. 97; *Strause Gas Iron Co. v. William M. Crane Co.*, 235 Fed. 126; *North British Rubber Co., Ltd. v. Racine Rubber Tire Co. of New York, Inc.*, 271 Fed. 936; *Weisgerber v. Clowney*, 131 Fed. 477; *Pashek v. Dunlop Tire & Rubber Co.*, 8 F. (2) 640.”

*Rowley v. Tressenberg et al.*, 37 Fed. Supp. 90 at 92, affirmed 123 F. 2d 844.

“\* \* \* To hold that general configuration made necessary by function must give to a patented design such breadth as to include everything of similar configuration, would be to subvert the purpose of the law, which is to promote the decorative arts rather than to effectuate it.”

*Applied Arts Corp. v. Grand Rapids Metalcraft Corp.*, 67 F. 2d 428 (C. C. A. 6).

“\* \* \* It has been held that a design patent cannot properly be obtained on the shape of a device which necessarily results from its mechanical parts.  
\* \* \* A statement pertinent to the instant situation was made in *Applied Arts Corp. v. Grand Rapids Metalcraft Corp.*, 67 F. 2d 428, wherein the court in discussing the design before it stated (page 430):

“‘In the main its configuration is made imperative by the elements which it combines and by the utilitarian purpose of the device. It was certainly not the intent of the law to grant monopoly to purely conventional design which is in itself little more than a necessary response to the purpose of the article designed.’”

*Circle S. Products Co. v. Powell Products, Inc., et al.*, 174 F. 2d 562 at 564 (C. C. A. 7).

“It is well settled that design patents should issue only upon ornamental or aesthetic features of a device, and cannot dominate functional or utilitarian features.”

*Connecticut Paper Products Inc. v. New York Paper Company*, 39 Fed. Supp. 127 at 134.

“\* \* \* Furthermore, it has been held that a purely functional design is not patentable. *S. Dresner & Son, Inc. v. Doppelt, et al.*, 120 F. 2d 50; *Applied Arts Corp. v. Grand Rapids Metalcraft Corp.*, 67 F. 2d 428, 430.

“\* \* \* The ampule being functional, it is difficult to perceive how its mere configuration could be other than functional.”

*Smith v. Dental Products Co., Inc. et al.*, 140 F. 2d 140 at 153 (C. C. A. 7) cert. den. 64 S. Ct. 1146, 322 U. S. 743.

“\* \* \* But the invention must relate to the design and be distinguishable from that which contrived the mechanical product for commercial purposes.”

*North British Rubber Co., Ltd. v. Racine Rubber Tire Co. of New York, Inc.*, 271 Fed. 936 at 938.

These rules were properly applied by the District Court. The only *ornamentation* shown in patent No. D143,641 is the round bead at the bottom of the V-shaped louver and this is **not used** by defendant. The only *ornamentation* shown in patent No. D138,990 is the specific design on the end consisting of the zig-zag, the outstanding trapezoidal housing cover and the recess and hemispherical boss therein. These are **not used** by defendant.



**PATENT NO. D143,641 [EXHIBIT 4; R. 343] IS  
LIMITED TO DETAILS BY FILE HISTORY  
LIMITATIONS AND BY THE PRIOR ART.**

The application for this patent was filed on July 28, 1944, and such application was rejected by the Patent Office on but a single reference, the "Challenger 77" fixture [Exhibit 9-H].

Applicants Biller and Kaepfel **admitted that there was no novelty** in their arrangement of the bottom of their louvers, stating on February 12, 1945:

"The 'Challenger' fixture, like applicants' fixture, has a bottom light-emitting opening provided with a louver construction including a central louver and a plurality of cross louvers." [R. 327.]

Patent No. D143,641 cannot be said to cover any and all combinations of longitudinal and transverse louvers because of this admission and because defendant's Exhibit I shows numerous prior art fixtures including louvers and baffles [R. 397, 399, 405, 412, 424, 443, 444, 447, 452, 454, 456, 469, 470, 471].

Biller and Kaepfel specifically limited their purported contribution to a V-shaped longitudinal louver which

"\* \* \* comprises upwardly diverging side walls connected by a longitudinal bottom bead or rib of circular cross section." [R. 327.]

Although they stressed this as an *ornamental* feature to the Patent Office, Kaepfel admitted on the stand that it was purely **utilitarian**.

"Q. What was the reason for the existence of that bead on the V-shaped louver? A. The bead came

into—was used in production for fastening the ends of the fixture to the longitudinal louver by means of a thread-cutting screw through the end plates.

Q. Did that circular bead on the V-shaped longitudinal louver contribute to its appealing appearance, in your opinion? A. No, sir.” [R. 68.]

Later, when the Patent Office again rejected their application, the applicants further limited their invention to a V-shaped louver made of “specular metal” [R. 330] and thereby distinguished from the white painted louvers such as are used by defendant here. Furthermore, applicants limited themselves to the use of “notched upper edges” on their cross louvers, stating that these notches are reflected in the specular sides of the V-shaped louver [R. 331].

Plaintiff is now estopped from claiming that the bead on the bottom of the V-shaped louver, shown in their patents, the use of specular metal and the notches in the upper edge of their cross louvers or baffles are not essential. They are the essential elements which caused the Patent Office to issue the patent. Kaepfel, one of the patentees, testified that the round bead is essential and had utility [R. 68, 112]. Since the head has utility, it was functional and not a proper element of a design patent.

The District Court correctly found that Patent D143,641 was limited to these details [Finding of Fact 3; R. 26]. The same details and limitations appear in Patent D138,990. Defendant **does not use** these details [Finding of Fact 10; R. 29].

PATENT NO. D138,990 MUST BE LIMITED TO  
THE SPECIFIC ORNAMENTATION ON  
THE END.

The only reference cited by the Patent Office in acting on this application was the "Challenger 77" fixture [R. 309].

It is fundamental that of two patents on the same subject, at least one of them must be invalid, as otherwise there is double patenting. Plaintiff admits in its brief that here we have "two patents upon a single louvered fluorescent lighting fixture" and stresses this anomalous situation in the headnote of page 32 of the brief.

"Only one valid, original patent can be granted to an inventor of one invention, and if a plurality of such patents are thus granted, all except the first are void. (Suffolk v. Hayden, 3 Wall. (70 U. S.) 315, 319, 18 L. Ed. 76; Miller v. Eagle Co., 151 U. S. 186, 197, 38 L. Ed. 121; Am. Steel Foundries v. Laughlin, 30 F. (2) 139, 142 (CCA 7 1928)."

*Walker on Patents, Deller's Edition*, page 1279.

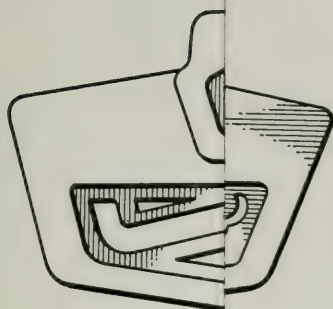
"Patentee cannot include in a later patent any invention described in a prior one."

*Farris v. Patsy Frock & Romper Co.*, 273 Fed. 900 (C. C. A. 9).

Patent No. D138,990 **cannot** cover the longitudinally extending baffle with its rounded beaded end nor the transverse baffles, because these elements are covered by the earlier filed patent No. D143,641. The invention, if any,

P  
PAT

Face



Face

Louver



Louver

End  
Section

End  
Section

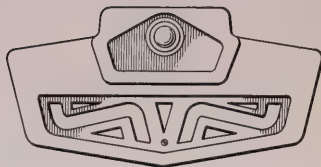




PLAINTIFF'S  
PATENT D-138,990

DEFENDANT'S  
FIXTURE

Face



Face



Different Design

Louver



No Bead



Louver

End  
Section



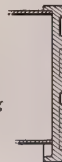
Raised

Two  
Piece

Flat

Single  
Casting

End  
Section





lies in the particular zig-zag ornamentation on the end of the device and, as stressed by the plaintiff, in the three parallel bars which connect the upper and lower rails of the inclined side panel. But the prior art clearly disclosed the use of one, two and three bars midway of an inclined side panel [see R. 385, 387, 395, 443, 456, 460, 471]. There is **no novelty** in such placement of bars.

The configuration of the end face of patent No. D138,990 in comparison with the end face used by defendant's "PARAMOUNT" fixture is shown on plate II. **That the design used by defendant is totally different was admitted** [R. 143, 113]. A tabulation of differences appears in the record, Vol. II, page 473. As correctly held by the District Court, if patent No. D138,990 is valid, it is not infringed, because **defendant does not use** the zig-zag design to which the patent is limited.

A comparison of Fig. 2 of patent No. 2,411,952 [R. 348] and patent No. D138,990 shows that the contours are identical, even to the raised, upper trapezoidal portion of the end. If Biller is the *sole* inventor of Fig. 2 of patent No. 2,411,952 and Biller and Kaepfel are *joint* inventors of patent No. D138,990, then obviously the only contribution made by Kaepfel was the zig-zag decoration. This emphasizes the fact that patent No. D138,990 must be limited to the specific zig-zag illustrated in the patent. Any attempt to cover the inclined sides, the step-down end or other functional features would necessitate holding the patent invalid, on the further ground that it was not issued to the true inventor.



DESIGN PATENTS MUST INVOLVE INVENTION. SINCE THE DESIGN OF THE PATENTS IN SUIT IS INSIGNIFICANT, THE PATENTS MUST BE STRICTLY LIMITED.

The District Court did not hold the design patents valid, but stated that if valid they were not infringed. Although the issue of validity is not directly in issue, the *quantum of invention* shown by the patentees should be considered. Invention is necessary as was stated by this Court in *Hammond v. Stockton Combined Harvester & Agricultural Works*, 70 Fed. 716 (cert. denied 16 S. Ct. 1202) and in later cases.

"It is well settled that a design patent must be the product of invention if it is to be valid. *Neufeld-Furst & Co. v. Jay-Day Frocks*, 2 Cir., 112 F. 2d 715; *In re Griffith*, C. C. P. A., 86 F. 2d 405. It will not suffice merely to show that the design is novel, ornamental, or pleasing in appearance. *Gold Seal Importers v. Morris White Fashions*, 2 Cir., 124 F. 2d 141. It must reveal a greater skill than that exercised by the ordinary designer who is chargeable with knowledge of the prior art. *Zangerle & Peterson Co. v. Venice Furniture Novelty Mfg. Co.*, 7 Cir., 133 F. 2d 266; *In re Eppinger*, C. C. P. A., 94 F. 2d 401. In short, the test is whether the design involved 'a step beyond the prior art requiring what is termed "inventive genius."' *A. C. Gilbert Co. v. Shemitz*, 2 Cir., 45 F. 2d 98, 99. So measured, plaintiff's patent must fail."

*General Time Instruments Corp. v. U. S. Time Corp.*, 165 F. 2d 853, 854 (C. C. A. 2), cert. denied 68 S. Ct. 1515, 334 U. S. 846.

Was it invention of an ornamental design to put a round bead on the end of the V-shaped louver, when such round bead was used as an attachment means and not as decoration? [R. 112]. Can a design patent on such invention be given any scope?

Was it “invention” to provide a zig-zag “doodle” on the end of the fixture? Can a design patent on such a simple, commonplace design be given any scope?

If it is assumed that these simple departures from the prior art constituted invention, then the patents must be **limited** to exactly what they show in their drawings.

**THE DESIGN PATENTS IN SUIT MUST BE  
STRICTLY CONSTRUED BECAUSE THE  
PRESUMPTION OF VALIDITY IS OVER-  
THROWN BY PRIOR ART.**

Plaintiff admits that the patents in suit were issued by the Patent Office after citation of only one prior publication, namely, the “Challenger 77” reference. The **Patent Office did not consider the numerous prior patents**, publications and fixtures shown in Exhibit I [R. 383, 471]. In view of these prior fixtures, which show that it was common practice to use inclined sides, step-down ends, louvered bottoms, and cut-outs in the end portions of fixtures, the presumption of validity no longer attaches to the design patents in suit, and the scope of the patents must be **limited** so as not to permit these design patents to cover what is in the prior art.

“\* \* \* But the presumption is overthrown beyond all reasonable doubt by the disclosures in evi-

dence before this court which were unknown and undisclosed to the Patent Office. *Alexander Anderson, Inc. v. Eastman*, 16 Fed. Supp. 515."

*Barkeij v. Ford Motor Company*, 22 Fed. Supp. 1001.

To the same effect, see *McClintock v. Gleason* (C. C. A. 9), 94 F. 2d 115; *Sidney Hollis Boynton v. Chicago Hardware Foundry Co.* (C. C. A. 7), 77 F. 2d 799, and *Mettler v. Peabody Engineering Corp., et al.*, 77 F. 2d 56 at 58 (C. C. A. 9), wherein the Court stated:

"The presumption of validity which attends the issuance of Letters Patent by the Patent Office is overcome in this case by the clear evidence of anticipation in the prior art which was not cited or considered by the Patent Office when the application for appellant's patent was passed on. See *Elliott & Co. v. Youngstown Car Mfg. Co.*, 181 Fed. 346 (C. C. A. 3); *American Soda Fountain Co. et al. v. Sample*, 130 Fed. 145 (C. C. A. 3)."

When a presumption of validity does not exist, it cannot be buttressed by obtaining two patents on the same subject.

## THE LAW REQUIRES THAT THE DESIGN PATENTS IN SUIT MUST BE LIMITED TO THEIR PRECISE SHOWINGS.

Design patents differ from patents on useful machines in that design patents have no descriptive matter. Ornamental designs would be difficult to describe, and reliance is placed upon the drawing. In the early case of *Zidell v. Dexter*, 262 Fed. 145, this Court held that the patentee of a design patent

**“\* \* \* must be held substantially to the design which he exhibits by his drawing.”**

This rule is followed in all circuits.

“On the other hand, the plaintiff’s patent, which contains no written description of his design, must be construed as limited to substantially the pattern shown in his drawings (*Ashley v. Tatum Co.*, 186 Fed. 339), \* \* \*. But if defendant’s changes result in producing a substantially different effect upon the eye, so that the two patterns are reasonably distinguishable, infringement will be avoided. *Zidell v. Dexter*, 262 F. 145; *Whiting Mfg. Co. v. Alvin Silver Co.*, *supra*.”

*American Fabrics Co. v. Richmond Lace Works et al.*, 24 F. 2d 365 at 367.

“The plaintiff’s design is restricted to the disclosure of the drawings, since there is no written specification: *Ashley v. Samuel C. Tatum Co.*, 186 F. 339; *American Fabrics Co. v. Richmond Lace Works*, 24 F. 2d 365, at 367; *Scoville Mfg. Co. v. United*



States Electric Mfg. Corporation, 31 F. Supp. 115, at 119.

“Every element in the design must be deemed to be essential: Dixie-Vortex Co. v. Lily-Tulip Cup Corporation, 95 F. 2d 461 at 467.”

*Forman v. American Express Company et al.*, 37 Fed. Supp. 82 at 83.

## PATENT NO. D143,641 IS NOT INFRINGED.

The drawings of this patent clearly show

(a) the **round bead** at the bottom of the V-shaped louver, such bead being represented to the Patent Office as an important element [R. 327];

(b) that **specular metal** is to be used for the V-shaped louver (indicated by shaded areas in Fig. 1) [R. 330];

(c) the **curved indentations** in the upper edge of the transverse baffles [R. 331].

**Defendant does not use these features.** [Admitted by Kaepfel, R. 112.] Plate II clearly points out the differences and facilitates comparison. The District Judge, in Finding 10, found that defendant does not use the bead nor does defendant use specular metal. Plaintiff does not contest this finding.

There is **no infringement** of patent No. D143,641 nor of corresponding parts of patent No. D138,990.

## PATENT NO. D138,990 IS NOT INFRINGED.

A comparison of the drawings of this patent with defendant's fixtures clearly shows that defendant does not use the zig-zag design. Plaintiff's own witnesses admitted that defendants' ornamentation was different [R. 142, 113]. Mr. Grossman listed all of the differences between plaintiff's and defendant's fixtures, and they appear in tabular form as Exhibit K [R. 473-474].

Non-infringement is so obvious that detailed discussion is unnecessary. Plaintiff cannot deny the facts. Finding of Fact 11 [R. 29] is a clear-cut statement which is uncontradicted by the evidence, and reads as follows:

"11. Defendant does not use, in its 'Paramount' fixtures exemplified by Exhibits 14 and 15, a zigzag design such as is shown in Letters Patent No. D-138,990; an entirely different design or ornamentation is used by defendant on its accused fixtures. Each of the step-down ends of defendant's fixtures are single castings which do not include a protruding upper portion. Defendant's fixtures do not employ the construction of plaintiff's fixtures and the louvered bottom is manipulated in a totally different manner. Defendant's fixtures, exemplified by Exhibits 14 and 15, employ forms and proportions which are common to lighting fixtures as a class and illustrated in prior art fixtures, and do not involve inventive change over the prior art."

The conclusion of law and judgment of non-infringement must be affirmed.

BY CHARGING DEFENDANT WITH UNFAIR COMPETITION, PLAINTIFF IS ATTEMPTING TO MONOPOLIZE NECESSARY AND FUNCTIONAL CONTOURS AND PROFILES OF LIGHTING FIXTURES.

Realizing that its design patents are not infringed, plaintiff is attempting to prevent defendant from making fixtures in which old, functional contours are used, by charging defendant with unfair competition. Defendant contends that anyone can make use of features which are necessary to the usefulness of the device. Anyone can use inclined, translucent sides to cast light downwardly and to the side, a step-down end to permit light to be emitted to the ceiling, and a louvered bottom to prevent glare.

“There is nothing about the article, as made and sold by the defendants, that is not necessary in the making and operation of such an instrument. *It is made in the form that it must be made in order to accomplish its purpose*, and, if the making in that form is any representation that the thing made came from the plaintiff, it is because of the extent to which the plaintiff had made and displayed and sold it before the defendants began.”

*Marvel Co. v. Tullar Co. et al.*, 125 Fed. 829 at 830.

“The plaintiff has not the exclusive right to sell shredded wheat in the form of a pillow-shaped biscuit—the form in which the article became known to the public.

“\* \* \* Moreover, the pillow-shape must be used for another reason. The evidence is persuasive that this form is functional—that the cost of the bis-

cuit would be increased and its high quality lessened if some other form were substituted for the pillow-shape.”

*Kellogg Company v. National Biscuit Company*,  
305 U. S. 111 at 119 and 122.

“Development in a useful art is ordinarily toward effectiveness of operation and simplicity of form. Carriages, bicycles, automobiles, and many other things from diversity have approached *uniformity through the utilitarian impulse*. If one manufacturer should make an advance in effectiveness of operation, or in simplicity of form, or in utility of color; and if that advance did not entitle him to a monopoly by means of a machine or a process or a product or a design patent; and if by means of unfair trade suits he could shut out other manufacturers who plainly intended to share in the benefits of the unpatented utilities and in the trade that had been built up thereon, but who used on their products conspicuous nameplates containing unmistakably distinct trade-names, trade-marks, and names and addresses of makers, and in relation to whose products no instance of deception had occurred—he would be given gratuitously a monopoly more effective than that of the unobtainable patent in the ratio of eternity to seventeen years.”

*Pope v. McCrum-Howell*, 191 Fed. 979, 981 (C. C. A. 7).

“It is attempted to sustain the cause of action for unfair competition on the ground that the defendants’ fruit juice extractors closely resemble those of the complainant \* \* \*. But there is no proof of palming off \* \* \*. Moreover, the elements of the fruit juice extractor are so far functional that noth-



ing short of a clear danger of confusion would justify us in requiring a modification of the model. *Crescent Tool Co. v. Kilborn & Bishop Co.* (C. C. A.), 247 F. 299; *Miller Rubber Co. v. Behrend* (C. C. A.), 242 F. 515.”

*A. C. Gilbert Co. v. Shemitz, et al.* (C. C. A. 2), 45 F. 2d 98 at 99-100.

“The complainant cannot obtain a monopoly for all time of perforated plates of the lengths having equidistant holes and intervening spaces which it first used. *These are functional features of the units of construction which any one is at liberty to use.*”

*Meccano, Ltd., v. John Wanamaker*, 250 Fed. 450 at 452 (C. C. A. 2).

Plaintiff does not have a patent on a lighting fixture having inclined side panels, a step-down end, and a louvered bottom. These are **necessary, functional features** which are common to all lighting fixtures and a **part of the prior art**. Defendant has the right to use these features. The use of such old features, necessary to perform the required functions, is not unfair competition. Counsel for plaintiff admitted that anyone can use such elements.

“Mr. Foster: \* \* \* I think the separate parts of any patented design which have mechanical utility, they are free for use by anyone” [R. 286].

Chief Justice Holmes, in *Flagg Manufacturing Co. v. Holway*, 178 Mass. 83, 59 N. E. 667, considered a case involving zithers, those made by the defendant so closely resembling the plaintiff's in outline, arrangement of strings, and other features, that it was obviously an imi-

tation. Chief Justice Holmes held that the defendant had a right to imitate the appearance of the plaintiff's zither, stating:

"Both zithers are adapted for the use of patented sheets of music, but the zithers are not patented. Under such circumstances the defendant has the same right that the plaintiff has to manufacture instruments in the present form, to imitate the arrangement of the plaintiff's strings or the shape of the body. In the absence of a patent the freedom of manufacture cannot be cut down under the name of preventing unfair competition. \* \* \* All that can be asked is that precautions shall be taken, so far as are consistent with the defendant's fundamental right to make and sell what he chooses, to prevent the deception which no doubt he desires to practice.

"It is true that a defendant's freedom of action with regard to some subsidiary matter of ornament or label may be restrained, although a right of the same nature with its freedom to determine the shape of the articles which it sells. But the label or ornament is a relatively small and incidental affair, which would not exist at all or at least would not exist in that shape but for the intent to deceive; whereas the instrument sold is made as it is, partly at least, because of a supposed or established desire of the public for instruments in that form. The defendant has the right to get the benefit of that desire even if created by the plaintiff. The only thing he has not the right to steal is the good will attaching to the plaintiff's personality, the benefit of the public's desire to have goods made by the plaintiff."

In commenting upon this case, Nims (the leading authority on unfair competition) stated:

“\* \* \* But the fact that the demand for zithers has been created by the plaintiff will not put the case within the unfair competition rules, where the demand is for the article, not the personality.”

*Nims on Unfair Business Competition*, page 290.

It is submitted that to sustain the charge of unfair competition, plaintiff must prove (1) that the article sold by plaintiff has acquired a secondary meaning and its shape is recognized as meaning that the article is made by plaintiff; that the public associates the non-functional, distinctive elements of appearance with plaintiff as the source of the fixture; and (2) that defendant has actually sold and palmed off upon the purchasing public a slighting fixture made by defendant as and for plaintiff's fixture.

This Court has succinctly stated the rule as follows:

“\* \* \* The law of unfair competition has resulted from the application of a simple proposition to the extension and modern development of manufacturing and merchandising. That principle may be expressed in the language used by the various courts when dealing with the subject of unfair competition, as follows: ‘That nobody has any right to represent his goods as the foods of somebody else.’ (Elgin Natl. Watch Co. v. Illinois Watch Co., 179 U. S. 665, 676.)”

*Del Monte Special Food Company v. California Packing Corporation*, 37 F. 2d 774 (C. C. A. 9).

Plaintiff has not proved secondary meaning nor palming off or deception. Plaintiff admitted that there was no evidence of secondary meaning.

“The Court: \* \* \* And I think I can say parenthetically here there is no direct evidence.

Mr. Foster: None direct.

The Court: That any customer in the trade associates the plaintiff's name with this type of fixture.

Mr. Foster: I think that is true” [R. 290].

The District Court found that there was no proof of secondary meaning [Finding of Fact 12, R. 29]. The District Court found that there was no palming off [Finding of Fact 13, R. 30]. Plaintiff does not object to these findings and cannot point to evidence to the contrary.

The District Court correctly applied the law to these facts and properly concluded that defendant is not guilty of acts of unfair competition. Any other conclusion would be contrary to the authorities.

### THE PURPORTED “COMMERCIAL SUCCESS” IS NOT ATTRIBUTABLE TO THE DESIGN SHOWN IN THE PATENTS.

Many pages of plaintiff's brief are devoted to commercial success, but this argument is fallacious for the following reasons:

1. The VIZ-AID fixture sold by plaintiff does not use the elements shown in the design patents. The VIZ-AID fixture **does not use** the characteristic round bead at the bottom of the V-shaped louver which is shown in both design patents in suit. The end of plaintiff's fixture does not include a recess (in the upper portion, constituting a cover for the ballast



housing) of the shape shown in patent D138,990. It does not use the hemispherical, concentrically ridged boss in such recess [R. 109].

2. The voluminous advertising of VIZ-AID fixtures is primarily directed to **mechanical features** which are covered by the mechanical patent No. 2,411,952. Many advertisements stress the snap-on enclosure whereby side panels, louvers and most of the ends can be dropped down and suspended from the ballast housing during relamping [R. 95, 175, 176; demonstrated by Kaepfel, R. 104; illustrated in Defendant's Exhibit A and Plaintiff's Exhibit 6K, R. 105]. This construction is covered by patent No. 2,411,952, Exhibit 5, R. 348. Plaintiff's witness admitted that **such construction is not used by defendant.**

"Q. That particular function or that particular arrangement, mechanical arrangement, cannot be found in the defendant's structure, can it? A. No." [R. 176.]

3. VIZ-AID advertising stresses the light distribution characteristics of the fixture, which certainly is not covered by design patents [R. 158-159].
4. The VIZ-AID fixture, as sold, includes, as a part of its design, embossing on three parallel bars on each side panel. This embossing is not shown in patent D138,990 [R. 108-109].

Therefore the commercial success of the VIZ-AID fixture is not attributable to the design patents, but to extensive advertising and to mechanical construction covered by other patents, not in suit here. Plaintiff did not attempt to state what percentage of its advertising stressed

functional details and mechanical construction and what percentage was directed to aesthetics and appearance [R. 176], because all of it is directed to matters *not covered* by the design patents in suit.

The argument regarding commercial success must be ignored because it is not pertinent. The issues here cannot be decided by plaintiff's ability to spend over \$88,000 in advertising; any such approach would always necessitate judgment for the party with most money.

The authorities clearly hold that commercial success cannot supplant invention. **Commercial success cannot convert non-infringement into infringement.**

### **THE MATHEMATICAL DISCOURSE OF PROFESSOR DOUGHERTY IS FOUNDED ON FALLACY AND HAS NO BEARING HERE.**

Plaintiff accuses defendant of infringing two patents; the issue is determined by applying the two design patents to defendant's structure.

Professor Dougherty did not do so. Instead, he compared plaintiff's commercial fixture with defendant's fixture. This is totally irrelevant because **plaintiff's commercial fixture does not embody what is shown in plaintiff's patents.**

Plaintiff's fixture does not use the round bead at the bottom of the V-shaped louver [R. 291]; plaintiff's fixture does not use the round protuberance in the recess of the cover plate at the end of the chassis [R. 109].

The Professor did not consider that defendant did not use the zig-zag design, and did not use the rounded bead on the V-shaped louver.

The entire premise of the mathematical exercise is therefore in error. Furthermore, the calculation of probabilities, as stated by Professor Dougherty, is based upon the assumption that each element [or marble in his example R. 132-133] is of exactly the same shape, weight and value. If not of the same value, then the mathematical method is not applicable, as admitted by the Professor [R. 141]. The Professor did not take into consideration that fact that prior art fixtures had inclined sides, step-down ends and louvered bottoms [R. 140]. He did not take into consideration that forty-eight inch tubes were common. These are old elements; they are common. He did admit, after looking at plaintiff's and defendants' fixtures

“Yes, I observe a difference in the appearance of the ornamental features, if that is what you have in mind” [R. 142].

That admission disposes of any contention that defendant infringes. If the ornamental features are different, defendant does not infringe.

**THE BURDEN OF PROOF WAS UPON PLAINTIFF. PLAINTIFF DID NOT AND COULD NOT SHOW CONFUSION, DECEPTION OR PALMING OFF.**

The commercial fixtures such as VIZ-AID and PARAMOUNT are **not sold to housewives** or the general public, but instead to engineers, purchasing agents for governmental bureaus, and architects. The fixtures are not dime store devices which are casually purchased without careful consideration; instead, the fixtures are **sold on specifications** as to light distribution, efficiency, etc. Defendant's fixtures, Exhibit 19, are sold under the name "PARAMOUNT."

Plaintiff could not and did not adduce testimony to show confusion, and failed to carry the burden of proof.

"\* \* \* In establishing such charge of unfair competition, we are of the view that plaintiff must show more than slight confusion—it *must be proved that the defendants palmed off their goods for that of the plaintiff*, and such proof must be by clear preponderance of the evidence. *Soft-Lite Lens Co., Inc., v. Ritholz*, 301 Ill. App. 100, 105."

*The Rytex Company v. Ryan, et al.*, 126 F. 2d 952 at 954 (C. C. A. 7).

"There is no showing in the record that any person purchased appellee's bait because of its shape, size or dimensions believing it to be the product of appellant. \* \* \* There is an entire absence of proof showing that appellee's bait of the design in



question had been bought because the purchaser believed it originated with appellant rather than because they were useful articles with an attractive appearance.”

*James Heddon's Sons v. Millsite Steel & Millsite Steel & Wire Works, Inc.*, 128 F. 2d 6 (C. C. A. 6).

“\* \* \* However, the mere existence of possible confusion does not give rise to the right of injunction. As stated by Judge Learned Hand in *Crescent Tool Co. v. Kilborn & Bishop Co.*, 247 F. 299, 300 (C. C. A. 2):

“‘. . . It is apparent that it is an absolute condition to any relief whatever that the plaintiff in such cases show that the appearance of his wares has in fact come to mean that some particular person—the plaintiff may not be individually known—makes them, and that the public cares who does make them, and not merely for their appearance and structure.’”

*The American Fork & Hoe Company v. Stampit Corporation* (C. C. A. 6), 125 F. 2d 472 at 475.

“\* \* \* Under the law of unfair competition a manufacturer is given protection for the distinctive dress or general appearance of his packages against a competitor who later enters the field with a device calculated to deceive the public and to enable the latter to palm off his goods for the goods of the former. *J. C. Penney Co. v. H. D. Lee Mercantile Co.*, 8 Cir., 120 F. 2d 949; *Queen Mfg. Co. v. Isaac Ginsberg & Bros., Inc.*, 8 Cir., 25 F. 2d 284. Here there is no evidence of confusion, deception or palming off, \* \* \*. \* \* \* The question of palming off, therefore, is one of probability only.

“\* \* \* When the rule of ensemble and general appearance is applied, and the elements which are common to the trade, such as bottles and labels of some sort, are considered, the resemblance is not sufficient to warrant a reversal of the trial court’s judgment.”

*The Seven Up Company v. Cheer Up Sales Company of St. Louis, Missouri, et al.* (C. C. A. 8), 148 F. 2d 909 at 912.

To the same effect:

*Wilhartz v. Turco Products Inc.*, 164 F. 2d 731 (C. C. A. 7);

*Ely Norris Safe Co. v. Mosler Safe Co.*, 62 F. 2d 524.

**THE CASES CITED BY PLAINTIFF ON PAGES 35-42 OF PLAINTIFF’S OPENING BRIEF ARE NOT PERTINENT TO THE FACTS IN THE INSTANT CASE.**

Upon analysis of the various cases cited by plaintiff, it will be found that, whenever the Court held that there had been unfair competition, there was evidence showing

- (1) that the article had acquired a **secondary meaning** and the public recognized the article as having its source with plaintiff;
- (2) that **non-functional**, decorative features had been copied;
- (3) that **actual deception** or palming off had occurred.

In the instant case there is no evidence of secondary meaning; defendant Ruby has not copied any decorative, non-functional features; and there is no evidence of deception.

Judge Learned Hand, in reviewing the various cases cited by plaintiff, while sitting in the Second Circuit in the case of *Crescent Tool Co. v. Kilborn & Bishop Co.*, 247 Fed. 299 (C. C. A. 2), stated at page 300:

“The cases of so-called ‘non-functional’ unfair competition, starting with the ‘coffee mill case,’ *Enterprise Mfg. Co. v. Landers, Frary & Clark*, 131 F. 240, 65 C. C. A. 587, are only instances of the doctrine of ‘secondary’ meaning. All of them presuppose that the appearance of the article, like its descriptive title in true cases of ‘secondary’ meaning, has become associated in the public mind with the first comer as manufacturer or source, and, if a second comer imitates the article exactly, that the public will believe his goods have come from the first, and will buy, in part, at least, because of that deception. Therefore it is apparent that it is an absolute condition to any relief whatever that the plaintiff in such cases show that the appearance of his wares has in fact come to mean that some particular person—the plaintiff may not be individually known—makes them, and that the public cares who does make them, and not merely for their appearance and structure. It will not be enough only to show how pleasing they are, because all the features of beauty or utility which commend them to the public are by hypotheses already in the public domain. The defendant has as much right to copy the ‘nonfunctional’ features of the article as any others, so long as they have not become associated with the plaintiff as manufacturer or source. The critical question of

fact at the outset always is whether the public is moved in any degree to buy the article because of its source and what are the features by which it distinguishes that source. Unless the plaintiff can answer this question he can take no step forward; no degree of imitation of details is actionable in its absence."

Furthermore, the *Rushmore v. Manhattan Screw* case, 163 Fed. 939, referred to by the plaintiff, was an appeal from an order granting a preliminary injunction, was not tried on the merits, contains a strong and logical dissent by Circuit Judge Noyes and commentary on this case indicates that the language of the decision is unfortunately general.

It is to be noted that in *Buckeye Incubator Co. v. Model Incubator Co.*, 237 Fed. 883, the Court found that the shape of the stove was *not* found in the prior art, "\* \* \* nor was it shown that such shaping was necessary to the performance of its functions." (P. 886.) Here, the prior art shows that the contour is old and common to many fixtures. The record shows that the inclined side panels **are necessary** to direct light angularly downward, the step-down end **is necessary** to permit light to be cast upwardly onto the ceiling and prevent undesirable contrast and the louvered bottom **is necessary** to prevent glare.

Defendant Ruby's "PARAMOUNT" fixture resembles the fixture of the expired Mitchell patent [R. 389]. It uses the V-shaped louvers such as shown in Masterson [R. 397], or illustrated in the Luminaire publication [R. 452, 460]. It uses a step-down end as shown in Illumination Engineering [R. 444], Luminaire, page 14 [R. 460], and Ruby's own 1941 fixtures [R. 373, 377, 469].



THE ADOPTION OF THESE CONTOURS, INCLINED SIDES, LOUVERS, ETC., COMMON TO LIGHTING FIXTURES, DOES NOT AMOUNT TO UNFAIR COMPETITION.

“\* \* \* any one was free to copy it so long as he did not attempt thereby to palm off his goods as those of complainant, and took due care to guard against any deception of the public into buying in the belief that it is purchasing complainant's goods.  
\* \* \* *And it results from this principle that the adoption by one manufacturer of the characteristic features of another's product, common to articles of that class, does not of itself amount to unfair competition.*”

*Rathbone, Sard & Co. v. Champion Steel Range Co.*, 189 Fed. 26 at 31 (C. C. A. 6).

“Both of the companies use similar bottles, boxes, and tins to contain the medicines prepared by them, and the cartons used to inclose them have a general correspondence in form and color. The labels on the containers and cartons are also of similar size and colors and have the same general style of letters. There is nothing unusual or distinctive in this dress of goods. Neither the use of the same colors, or of the same form of containing vessels, cartons, or labels, alone constitute unfair competition, when such features are in common use in the trade, and especially when these features serve purposes of utility, convenience, or attraction. *P. Lorillard Co. v. Peper*, 86 Fed. 956, 30 C. C. A. 496; *Globe-Wernicke Co. v. Fred Macey Co.*, 119 Fed. 696, 56 C. C. A. 304; *Marvel Co. v. Pearl*, 133 Fed. 160, 66 C. C. A. 226; *Sterling Remedy Co. v. Eureka Chemical & Manufacturing Co.*, 80 Fed. 105, 25 C. C. A. 314.”

*Viazi Co. v. Vimedia Co.*, 245 Fed. 289 at 293.

It is submitted that the cases relied upon by plaintiff are not only distinguishable from the facts of the instant case for the reasons stated, but furthermore, fail to reflect the weight of authority and tenor of the decision of the Supreme Court of the United States, as expressed in *Kellogg Co. v. National Biscuit Co.*, 305 U. S. 111.

In that case, National Biscuit Company sued Kellogg for (1) unfair competition in selling a pillow-shaped breakfast food and (2) calling it "Shredded Wheat". Mr. Justice Brandeis delivered the opinion, stating that Kellogg:

"\* \* \* contends that in honestly competing for a part of the market for shredded wheat it is exercising the common right freely to manufacture and sell an article of commerce unprotected by patent." (P. 116.)

On secondary meaning the Court stated:

"\* \* \* There is no basis here for applying the doctrine of secondary meaning. The evidence shows only that due to the long period in which the plaintiff or its predecessor was the only manufacturer of the product, many people have come to associate the product, and as a consequence the name by which the product is generally known, with the plaintiff's factory at Niagara Falls. But to establish a trade name in the term 'shredded wheat' the plaintiff must show more than a subordinate meaning which applies to it. *It must show that the primary significance of the term in the minds of the consuming public is not the product but the producer.* This it has not done." (P. 118.)

On the right of all to use old forms, the Court stated:

"The plaintiff has not the exclusive right to sell shredded wheat in the form of a pillow-shaped biscuit

—the form in which the article became known to the public. That is the form in which shredded wheat was made under the basic patent. \* \* \* Hence, upon expiration of the patents the form, as well as the name, was dedicated to the public. \* \* \*

“Where an article may be manufactured by all, a particular manufacturer can no more assert exclusive rights in a form in which the public has become accustomed to see the article and which, in the minds of the public, is primarily associated with the article rather than a particular producer, than it can in the case of a name with similar connections in the public mind. *Kellogg Company was free to use the pillow-shaped form, subject only to the obligation to identify its product lest it be mistaken for that of the plaintiff.* (Pp. 119-120.)

“Moreover, the pillow-shape must be used for another reason. The evidence is persuasive that *this form is functional*—that the cost for the biscuit would be increased and its high quality lessened if some other form were substituted for the pillow-shape.” (P. 122.)

The *Kellogg* case reiterates the right of all to use common forms and to compete for business. In a more recent case, *Gum, Inc. v. Gumakers of America, Inc.*, 136 F. 2d 957 (C. C. A. 3), plaintiff packaged bubble gum in cylindrical form for ten years before defendant produced bubble gum, also in cylindrical form. The Court held that defendant had the right to make bubble gum of this particular shape, stating:

“Aside from the prohibition against infringing a patent, copyright or trade mark and except for the requirement, hereinafter discussed, that he must identify his product as his own, *any one has the right to manufacture and sell a product similar or even*

*identical in appearance to the original product with which it competes* unless the original product has become associated in the public mind with its producer. (P. 958.)

“From this evidence it would be possible to conclude that the plaintiff by its pioneer work in the field created the desire in the public for bubble gum having the appearance of Blony, that the defendant copied that appearance and profited by the public demand which the plaintiff had aroused. This evidence would not, however, justify a finding that the public associates with the plaintiff bubble gum having the appearance of Blony in the form in which it is marketed or that the public demand is for the plaintiff’s product as such.” (P. 960.)

In *The Zangerle & Peterson Company v. Venice Furniture Novelty Manufacturing Company*, 133 F. 2d 266 (C. C. A. 7), the Court stated:

“In the absence of actual ‘palming off’ or the existence of a secondary meaning in the trade, the copying by the defendant of the plaintiff’s unpatented design did not amount to unfair competition. Where no one has the exclusive right to the use of a design, all may use it with impunity, so long as the public is not misled in the methods of marketing the product.”

The correct rule of law is: That Defendant Ruby, in common with other manufacturers of lighting fixtures, has the right to use those shapes, angles, contours and materials which are **functionally necessary to properly distribute light**. Defendant’s only duty is to refrain from copying non-functional, decorative or ornamental, patented features, and from palming off its goods as the goods of plaintiff.



## THE TRIAL COURT PROPERLY AWARDED DEFENDANT TAXABLE COSTS AND AT- TORNEYS' FEES.

Pursuant to 35 U. S. C. A. 70, the District Court awarded a portion only of the attorneys' fees actually incurred by defendant. The award of attorneys' fees is discretionary with the Trial Court. Senate Report No. 1502, June 14, 1946, adopted from a report of the House Committee on Patents, in discussing this provision stated:

"The provision is also made general so as to enable the court to prevent a gross injustice to an alleged infringer."

Long prior to the amendment of 35 U. S. C. A. 70 the courts have awarded attorneys' fees and costs in addition to the normal costs taxable as a matter of course, whenever it appeared that a party made unfounded representations, unnecessarily prolonged trial, took depositions unnecessarily, or otherwise placed an oppressive burden upon the opponent.

In the instant case, the plaintiff, one of the most powerful manufacturers of lighting fixtures, and who apparently manufactures about one-fourth of the nation's output in fluorescent tube fixtures, sued a small manufacturer. It is submitted that plaintiff's counsel have gone to great lengths in aggressively establishing its position; plaintiff has gone to the length of obtaining two design patents upon a single fixture, but it is submitted that plaintiff's counsel, thoroughly familiar with plaintiff's patents, their file histories and the prior art, **should have realized that defendant did not infringe and did not use essential elements of these design patents.** Defendant therefore contends that plaintiff did not have a justifiable cause for prosecuting the action.

The Trial Court in the instant case took into consideration the fact that plaintiff charged defendant with infringement of patent No. 2,411,952 by notice in August, 1947 [Finding No. 2, R. 25]. **There was no basis for such charge** and plaintiff's own witness admitted that defendant did not use the construction covered by this patent [R. 176]. However, defendant was forced to study this patent, investigate the prior art, and prepare thereon. In June, 1948, the complaint filed by the plaintiff left out this mechanical construction patent No. 2,411,952 and limited the charge of infringement to the two design patents.

The complaint made unsupportable and unjustifiable allegations. For example, paragraph XIII of the complaint [R. 5] alleged that "plaintiff has placed the required statutory notice upon all lighting fixtures sold by plaintiff." However, upon trial, plaintiff's own witness, Kaepfel, admitted that the fixtures were not marked with patent numbers.

"Q. (By Mr. Miketta): Are there any patent numbers that are marked or engraved on that fixture?  
A. There are none that I know of." [R. 96.]

Why did plaintiff make an unjustifiable allegation in its complaint regarding its own fixtures?

The record of this case further shows that plaintiff took depositions of five of defendant's officers and employees, which depositions were not introduced into evidence during the trial. The taking of these depositions caused defendant to incur loss of time and increased the expense imposed upon defendant.

The Trial Court had opportunity to observe the witnesses, to hear all of the arguments and to listen to and

weigh all of the contentions made. The Trial Court observed that **plaintiff waited one year and nine months after the complaint was filed** and waited until the plaintiff had **closed its prima facie case** before plaintiff amended its complaint to introduce a totally new charge, that of unfair competition.

Did the Trial Court abuse its discretion in mentioning this late charge in Finding of Fact 2 and in considering such tactics in awarding attorneys' fees?

Defendant's counsel filed an affidavit [R. 23-24] specifying the work done and the hours of time spent on this case. The legal services of defendant's counsel and his associate averaged about \$15 per hour in gross and amounted to \$6,240, with an additional \$684.13 for reporters' fees, exhibits, file histories, etc., making a total of \$6,924.13. The Trial Court awarded defendant only \$3,000 in attorneys' fees and reporters' fees and costs were taxed at \$388.99. Certainly this does not compensate defendant for the lost time, the disruption of defendant's normal business operations, the harmful effect on defendant's business due to knowledge by the trade that defendant was being sued by one of the most powerful companies in the lighting fixture industry. The Senate Report stated that the purpose of Section 70 was "\* \* \* to prevent a gross injustice to an alleged infringer."

From the record in this case and from the findings of fact made by the District Court, it is evident that the Trial Judge had considered the tactics employed by plaintiff and the actual expenditures incurred and, in the Court's dis-

cretion, made an award of less than one-half of such actual expenditures. This was not an abuse of discretion.

“We think it clear that under the statute the question is one of discretion. The court exercised its discretion and that ends the matter, unless we can say, as a matter of law, that there was a clear abuse of discretion. This we cannot say.”

*Blanc v. Spartan Tool Co.*, 168 F. 2d 296 (C. C. A. 7).

This Court, in the recent case of *Dubil v. Rayford Camp & Co.* (decided October 18, 1950, 87 U. S. P. Q. 143) had indicated that it is better practice for the Trial Court to make a specific finding as to the basis of its conclusion to award attorneys' fees. In the *Dubil* case the matter was complicated by the fact that Federal and non-Federal causes had been joined and there was no evidence to show how much of counsel's time had been spent on the non-Federal cause of action. Moreover, one of the defendants was not chargeable with elements of fraud. In the instant case the record is clear; non-infringement should have been apparent to skilled counsel for plaintiff; there was no excuse for the belated charge of unfair competition (apparently made in an attempt to catch defendant by surprise during trial); and the findings of fact and record disclose grounds upon which an award is justified. It is to be noted that the award is only one-fifth of that in the *Dubil* case.

It is therefore submitted that the findings justify the award, and adequately state a basis therefor.



## SUMMARY AND CONCLUSION.

Defendant, Ruby Lighting Corporation, has presented FACTS, which clearly establish

- (1) that all lighting fixtures (from a date long prior to the filing of the patents in suit) have functional, necessary and common shapes and elements;
- (2) that the art has used such shapes and elements and must use them to get lighting efficiency;
- (3) that the patents in suit, if valid, are extremely limited;
- (4) that defendant has not used the purported ornamental features of the design patents in suit.

LAWPOINTS AND AUTHORITIES which establish

- (1) that design patents must be limited to what is shown in their drawings;
- (2) that the use of features common to articles of a class, particularly when such features are utilitarian, is free to all;
- (3) that to sustain an action for unfair competition plaintiff must prove palming off, deception of customers, or that the public associates the particular product with plaintiff as the source (*Kellogg Co. v. National Biscuit Co.*, 305 U. S. 111).

Defendant, Ruby Lighting Corporation, submits:

- (1) that plaintiff failed to show secondary meaning, palming off or deception;
- (2) that the Findings of the District Court adequately support the Judgment;
- (3) that the Judgment of the District Court be affirmed and the appeal dismissed, with costs to the defendant.

DATED: At Los Angeles, California, this 22nd day of December, 1950.

Respectfully submitted,

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No. 12633.

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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DAY-BRITE LIGHTING, INC., a corporation,  
*Plaintiff-Appellant,*  
*vs.*

RUBY LIGHTING CORPORATION, a corporation,  
*Defendant-Appellee.*

---

## REPLY BRIEF FOR PLAINTIFF-APPELLANT.

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*Plaintiff-Appellant,*

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RUBY LIGHTING CORPORATION, a corporation,

*Defendant-Appellee.*

---

## REPLY BRIEF FOR PLAINTIFF-APPELLANT.

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This brief is in reply to "Brief for Appellee." The chief points raised by defendant in such brief are answered herein *seriatim*.

### Summary of Argument.

A. THE TWO DESIGN PATENTS IN SUIT ARE INFRINGED.

1. That Various Appearance Features of a Patented Device May Also Perform a Useful Function Does Not Exclude Such Features From Forming Part of the Design Thereof.
2. The Design Patents in Suit Are Not Limited in Scope by File-Wrapper Estoppel.
3. No Limited Construction of the Design Patents in Suit Is Required by the Prior Art.



B. IT IS UNFAIR COMPETITION TO COPY THE APPEARANCE OF AN ARTICLE NOT DICTATED AND FROZEN BY MECHANICAL AND USE REQUIREMENTS WHERE SUCH APPEARANCE HAS ACQUIRED A SECONDARY MEANING.

1. Defendant Has Duplicated Numerous Features of Plaintiff's Fixture Which Are Not Dictated by Requirements of Use.
2. The Appearance Features of Plaintiff's Fixture Have Acquired a Secondary Meaning.
3. No Proof of Actual Confusion or Damages to Plaintiff Need Be Presented to Establish Unfair Competition.

C. DEFENDANT HAS NOT ESTABLISHED ANY SPECIAL CIRCUMSTANCES ENTITLING IT TO ATTORNEYS' FEES.

D. CONCLUSION.

## ARGUMENT.

A. The Two Design Patents in Suit Are Infringed.

Defendant has sought to avoid infringement of the design patents in suit by ascribing functionality to the many features of plaintiff's lighting fixture which it has directly appropriated and by limiting the patents in scope to coverage of only the few minute details which differentiate the accused fixture from the design shown in the patents in suit. No such limitation in the scope of the patents is warranted by the file histories of the patents, the prior art, or the nature of the elements forming the patented fixture.

**1. That Various Appearance Features of a Patented Device May Also Perform a Useful Function Does Not Exclude Such Features From Forming Part of the Design Thereof.**

Defendant asserts that except for the round bead on the bottom of the V-shaped louver in Patent No. D-143,641 and zig-zag end design in Patent No. D-138,990, the balance of the features is functional and not subject to design patent coverage. (Deft. Br. pp. 6-11.)

That the design patents may not be properly limited to include only those parts or elements which are devoid of utility is well established. In the frequently-cited decision of *Ashley v. Weeks-Numan Co.*, 220 Fed. 899 (C. C. A. 2, 1915), the rule is stated, page 901:

“ . . . In a design patent the appearance is the subject-matter of the patent, and the appearance is none the less patentable because a mechanical function is involved. The patentability of a design is determined by its appeal to the eyes, and not by the presence or absence of a mechanical function.”

**2. The Design Patents in Suit Are Not Limited in Scope by File-Wrapper Estoppel.**

Defendant asserts that Patent No. D-143,641 is limited by its file history to the use of a V-shaped louver having a longitudinal bottom bead of circular cross section, made of specular metal and having notches in the upper edges of their cross louvers or baffles. Patent No. D-138,990, it is contended, is similarly limited to the particular zig-zag ornamentation on the end of the device. (Deft. Br. pp. 12-15.)

Defendant also insists that the scope of the invention be whittled down by the requirement that each of these so-called limitations be found in the infringing article, a practice which has been repeatedly frowned upon by the courts and was recently condemned by the Supreme Court in *Graver Tank & Mfg. Co., Inc. v. The Linde Air Products Company*, 94 L. Ed. 767 (Advance Opinions).

The statement made by applicants Biller and Kaepfel during the prosecution of Patent No. D-143,641 regarding the basic similarity of the "Challenger" fixture and the fixture of their invention [R. 327] merely conceded that the "Challenger" fixture included the general *mechanical* arrangement of the applicants' invention but did not concede design similarity or identity.

Never, at any time during the prosecution of Patent No. D-143,641, did the applicants limit their contribution to the longitudinal bead on the bottom of the V-shaped louver. As a matter of fact, applicants repeatedly stressed the fact that their contribution lay in a fixture which included ". . . a wide V-shaped central longitudinal louver with downwardly converging sides" [R. 330]. *Any references made to the longitudinal bead did not partake of the nature of limitation but of description.*

The contention that the patentees limited the use of the invention to "specular metal" is based upon references made by the applicants to a copending mechanical application in which the use of such metal was disclosed. In the design application, applicants did not limit the use of the invention to any particular material but indicated that the appearance features of the device would be *enhanced* by the use of such a material.

As indicated previously, applicants repeatedly stressed the shape of the V-shaped central louver and the single statement during the prosecution of the application regarding the “notched upper edges” of the cross louvers was merely intended to point out an additional feature of novelty in the design.

Therefore, the attempts of the defendant on the basis of the file-history estoppel to limit Patent No. D-143,641 to a bead on the bottom of the V-shaped louver, the use of specular metal and the notches in the upper edges of the cross louvers are without support in said file history. The Patent Office issued the patent because the overall design disclosed was broadly distinguished over the “Challenger” reference.

Defendant contends that Patent No. D-138,990 must be limited to the specific ornamentation on its ends because the V-shaped louver is covered by Patent No. D-143,641. However, the relationship of Patent No. D-138,990 to Patent No. D-143,641 is that of a combination patent to a sub-combination patent. Because the V-shaped louver disclosed in “641” was a design unit in itself, it was separately claimed and patented. However, this did not estop the plaintiff from independently patenting a design of which the V-shaped louver constituted a component part.

No representations to the Patent Office were made in the prosecution of this patent application and it was immediately allowed. The file history of the application cannot, therefore, introduce any limitations but, on the contrary, the patent covers the entire design disclosed.



### 3. No Limited Construction of the Design Patents in Suit Is Required by the Prior Art.

Defendant contends that the presumption of validity attending the grant of the patents in suit is overcome by failure of the Patent Office to cite all the prior art shown in Exhibit I and that the patents must therefore be strictly construed. (Deft. Br. pp. 17-18.)

In the prosecution of both applications the Patent Office cited as a reference the "Challenger 77" fixture, Exhibit 9-H. As may be observed by even a casual inspection thereof, this reference is far closer in appearance to the fixtures pictured in the design patents in suit than is any of the prior art shown in Exhibit I. The trial court found no reference to be more pertinent than the "Challenger 77."

By exhibiting prior art *less pertinent* than that before the Patent Office during the prosecution of the patents in suit, plaintiff cannot destroy or weaken the presumption of validity attending the grant of the patents, and, in fact, such presumption is thereby strengthened.

"The best reference cited by the defendant as the nearest approach to Hibbard was the Maxwell patent. No. 1,089,659 issued to the defendant March 10, 1914. This patent was considered and rejected by the Patent Office in connection with the Hibbard application, thereby strengthening the regular presumption of validity of the Hibbard patent. *Smokador Mfg. Co. v. Tubular Products Co.* (C. C. A.), 31 F. (2d) 255, 257; *Elkon Works v. Welworth Automotive Corporation* (D. C.), 25 F. (2d) 968, 970."

*Electric Machinery Mfg. Co. v. General Electric Co.*, 13 Fed. Supp. 940, 942 (D. C., S. D. N. Y.) (1936). (Modified and affirmed, 88 F. 2d 11, C. C. A. 2, 1937.)

**B. It Is Unfair Competition to Copy the Appearance of an Article Not Dictated and Frozen by Mechanical and Use Requirements Where Such Appearance Has Acquired a Secondary Meaning.**

Although it is a general rule of law that anyone may, without liability, copy features of appearance of an unpatented article which are dictated solely by mechanical or use requirements, features of appearance in the form, structure or general arrangement of an article which are not dictated and frozen in their precise form by mechanical and use requirements, but which are selected to and do render it attractive and distinguishable from other like articles, are subject to a different rule.

In such cases, where the article is identified as to its source by its general appearance of form, shape, and general arrangement of parts, the courts have long condemned the copying as unfair as indicated by the decisions cited in Plaintiff-Appellant's Opening Brief, pages 35-42. The rationale of the rule is simple: whereas appearance features, required to be in the form presented by the use of the device and its commercial acceptance and success, must necessarily be employed by anyone making a similar unpatented device, appearance features not dictated in the form presented by use are copied without necessity and only for the obvious purpose and with the obvious result of confusion and deception of the buyer.

**1. Defendant Has Duplicated Numerous Features of Plaintiff's Fixture Which Are Not Dictated by Requirements of Use.**

Defendant's brief stresses the point that certain particular elements of any light fixture, such as an inclined side panel, a step-down end, or a louvered bottom, are features related to the usefulness of the device the copy-

ing of which does not constitute unfair competition. In support of this contention are cited several authorities holding that the appropriation of a shape or form which is *required* to be used for utilitarian purposes is not wrongful. (Deft. Br. pp. 22-25.)

This argument does not meet the evidence presented in this case, which proves that defendant not only used numerous so-called decorative features of plaintiff's fixture but duplicated various functional parts down to the last minute detail of dimensions, angles and arrangements, although such dimensions, angles or arrangements were not dictated by the necessity of producing an operative fixture.

It was obviously not utilitarian requirements which caused defendant's fixture to coincide precisely with plaintiff's fixture in cut-off angle, for example, which might have been varied between  $25^{\circ}$  and  $38^{\circ}$  without affecting the utility of the fixture [R. 124-125]; nor was it necessary that the length of both the devices be identically fixed at 48 7/16" to insure utility [R. 126, 278]; nor that the defendant's fixture be of exactly the same overall height or depth as plaintiff's [R. 125, 276-277]. Although both fixtures contained the same number of louvers (13), any number between 8 and 29 might have been employed by defendant without affecting utility [R. 125-126].

No less condemned by the courts as unfair competition is the duplication of the appearance features of a device which serve a useful purpose, rather than the purely decorative features, where, as in the instant case, such *useful appearance features might have been varied over a wide choice of dimensions without affecting the utility of the accused structure.*

In *Luminous Unit Co. v. R. Williamson & Co.*, 241 Fed. 265 at 269 (D. C. Ill. 1917), affirmed 245 Fed. 988 (C. C. A. 7, 1917), which case also involved copying of a light fixture, the Court stated:

“ . . . Defendant tried to find an equivalent form which would not so closely resemble the other, but, finding it difficult to do this in respect to the canopy, concluded to adopt the device as a whole. The *exact shape* of the bowl is not *functional*, nor its *markings*, nor the *number and style of hangers*, . . . Defendant could have so changed its device as to avoid this confusion, without interfering with economic, structural, or functional requirements, because there is nothing in the shape of the bowl which is essential. This is a clear case of implied or circumstantial proof of misrepresentation of origin. . . .”  
(Emphasis added.)

See also:

*Thayer Telkee Corporation v. Davenport-Taylor Mfg. Co.*, 46 F. 2d 559 (D. C., N. Y., 1930) (Pltf-App. Op. Br. p. 39);

*McGill Mfg. Co. v. Leviton Mfg. Co.*, 43 F. 2d 607 (D. C., N. Y., 1930) (Pltf-App. Op. Br. pp. 37-39).

## 2. The Appearance Features of Plaintiff's Fixture Have Acquired a Secondary Meaning.

Defendant asserts in its brief that no secondary meaning is established because no *direct* evidence of association by customers with plaintiff's name was adduced. (Pltf.-App. Op. Br. p. 27.) The trial court's Finding of Fact No. 12 [R. 29] is apparently based on the erroneous assumption that secondary meaning is established only by direct testimony of customers and the uncontroverted in-



direct proof thereof is disregarded. Actually, plaintiff's indirect proof of secondary meaning is far more persuasive than would be the testimony of such customers as might have been called upon by both sides, in endless array, to testify to their association or lack of association of plaintiff's name with the distinctive appearance of its product.

That secondary meaning may be established as a result of such indirect evidence as extensive advertising, sales and long usage has been frequently held by the courts and writers in the field of unfair competition. For example, see:

*Nims on Unfair Competition & Trademarks*, 4th Ed., Sec. 344, pages 1038-1040;

*Wisconsin Electric Co. v. Dumore Co.*, 35 F. 2d 555 (C. C. A. 6, 1929);

*Pro-phy-lac-tic Brush Co. v. Abraham & Straus*, 11 Fed. Supp. 660 (D. C., N. Y., 1935);

*F. W. Fitch Co. v. Camille*, 106 F. 2d 635 (C. C. A. 8, 1939);

*Shaler Co. v. Rite-Way Products, Inc.*, 107 F. 2d 82 (C. C. A. 6, 1939);

*General Shoe Corporation v. Rosen*, 111 F. 2d 95 (C. C. A. 4, 1940);

*Prince Matchabelli, Inc. v. Anhalt & Co., Inc.*, 40 Fed. Supp. 848 (D. C., N. Y., 1941).

In the last-cited case, wherein the facts appear quite similar to those of the instant case, the Court stated, page 850:

“ . . . The affidavits of the plaintiff show that the plaintiff has been engaged for more than fifteen years in the manufacture and sale of perfumes, cosmetics and related articles, such as compacts, purse

kits and the like; these articles have been put out by the plaintiff in a distinctive way so as to show their origin, and have been extensively advertised; they have always borne the name and mark of the plaintiff, and have become identified by the public as the plaintiff's product. It is also stated in the affidavits that approximately \$50,000.00 has been spent for advertising and promoting the purse kit of the patent, and that 282,732 of the purse kits have been sold at \$1 each, representing a retail sales value of \$282,732. None of these facts has been questioned or denied in the affidavits submitted by the defendant. . . .

"I think it is plain from the record now before me that the purse kit of the patent has 'become so associated with the plaintiff in the mind of the public as to acquire a secondary meaning and cause any bag of the same appearance to be ascribed to the plaintiff as the source of production.' . . ."

**3. No Proof of Actual Confusion or Damages to Plaintiff Need Be Presented to Establish Unfair Competition.**

Defendant in its brief stresses the fact that plaintiff has failed to show proof of actual deception or palming off. (Pltf.-App. Op. Br. pp. 33, 39.) This Court, as well as numerous California decisions, has held *the mere likelihood of confusion or damage to plaintiff is sufficient.*

*Stork Restaurant, Inc., v. Sahati*, 166 F. 2d 348 (C. C. A. 9, 1948);

*Sun-Maid Raisin Growers v. Mosesian*, 84 Cal. App. 485, 258 Pac. 630;

*California Prune & Apricot Growers Association v. Nicholson*, 69 Cal. App. 2d 207, 65 U. S. P. Q. 533;

*Winfield v. Charles*, 77 Cal. App. 2d 64, 175 P. 2d 69.

In the *Winfield* case the Court stated the rule in unfair competition cases as follows:

“*It is unnecessary*, in such an action, to show that any person has been confused or deceived. It is the likelihood of *deception* which the remedy may be invoked to prevent.” (Emphasis added.)

### C. Defendant Has Not Established Any Special Circumstances Entitling It to Attorneys’ Fees.

Defendant in its brief attempts to enumerate several circumstances which it alleges justify the Court in awarding attorneys’ fees to it. These are a far cry from the type of finding which this Court recently indicated might justify such an award in *Dubil v. Rayford Camp & Co.*, 87 U. S. P. Q. 143, namely, fraud in the inducement of the patent or unreasonable prolongation of the trial.

Defendant’s principal contention is that non-infringement should have been apparent to plaintiff’s counsel (Pltf.-App. Op. Br. p. 43), so they should never have brought the suit in the first instance, *i. e.*, the action was unjustifiably commenced. This argument is obviously specious, patent infringement being almost always a question which is wide open to an honest difference of opinion.

Plaintiff’s conduct in charging infringement of a third patent, No. 2,411,952, and failing to sue thereon (Deft. Br. p. 41) shows a restraint in bringing to the trial claims which plaintiff felt might not be fully substantiated. Undue prolongation of the trial was actually avoided by plaintiff in suing under the design patents only.

The fact that depositions were taken by plaintiff and not introduced into evidence (Pltf.-App. Op. Br. p. 41) is not reprehensible conduct on the part of plaintiff, since

the depositions were taken as provided by the Federal Rules of Civil Procedure for discovery purposes and not for use as evidence at the trial. The amendment of the complaint to introduce the unfair competition count, which defendant emphasizes was made after the close of plaintiff's *prima facie* case (Deft. Br. pp. 41-42), did not prolong the proceedings but merely conformed the pleadings to the proof.

In short, defendant cannot point to any facts regarding defendant's conduct throughout this litigation which justifies a holding of "special circumstances" and the trial court made no findings of fact whatsoever to support the same. The trial court obviously felt that attorneys' fees should be given to the prevailing party in any patent suit, and irrespective of the fact that the equities lay with the losing party, and thereupon awarded a substantial sum to defendant as a matter of course. It is submitted that in making such award the trial court clearly abused its discretion.

#### **D. Conclusion.**

Defendant does not attempt to disprove the fact that the accused device and the device of the patents are indistinguishable except in minute detail, on very close scrutiny. Instead, defendant seeks to place unwarranted limitations on the patents in suit in an effort to nullify completely the protection afforded under the Patent Laws to new, original and ornamental designs.

In addition, defendant has appropriated numerous appearance features of plaintiff's device down to the smallest detail of form and dimension, such features being identified among consumers with plaintiff and its product.



All the equities of this case lie with plaintiff. Merely because defendant has prevailed in the trial court is no basis for penalizing plaintiff by an award of attorneys' fees to defendant.

It is accordingly respectfully submitted that the decision of the trial court should be reversed.

Dated: At Los Angeles, California, this 4th day of January, 1951.

Respectfully submitted,

CARR & CARR & GRAVELY,  
JOSEPH J. GRAVELY,  
HARRIS, KIECH, FOSTER & HARRIS,  
FORD HARRIS, JR.,  
WARREN L. KERN,  
*Attorneys for Plaintiff-Appellant.*

No. 12634

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United States  
Court of Appeals  
for the Ninth Circuit.

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UNITED STATES OF AMERICA,

Appellant,

VS.

DOROTHY SHARP,

Appellee.

---

Transcript of Record

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Appeal from the District Court of the United States  
Southern District of California,  
Central Division.

FILED

NOV 21 1950

PAUL P. O'BRIEN,

CLERK



No. 12634

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United States  
Court of Appeals  
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UNITED STATES OF AMERICA,

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Southern District of California,  
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

### For Appellant:

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1206 Santee St.,  
Los Angeles 15, Calif.

### For Appellee:

MATOT, GABRIELSON & MANLEY,  
715 Loew's State Bldg.,  
707 S. Broadway,  
Los Angeles 14, Calif. [1]

In the United States District Court, Southern District of California, Central Division.

No. 9996-B

UNITED STATES OF AMERICA,

Plaintiff,

vs.

DOROTHY SHARP, DOES I to X,

Defendants.

COMPLAINT FOR TREBLE DAMAGES,  
RESTITUTION AND INJUNCTION

I.

Plaintiff brings this action for restitution pursuant to Section 205(a) of the Emergency Price Control Act of 1942, as amended, and brings this action also for injunction, restitution and treble damages pursuant to Sections 205 and 206 of the Housing and Rent Act of 1947, as amended, (Public Law 31, 81st Congress, 1st Session).

II.

Jurisdiction of this action is founded upon Section 205(c) of the Emergency Price Control Act of 1942, as amended, and Section 206 of said Housing and Rent Act of 1947, as amended. [2\*]

III.

At all times mentioned herein prior to July 1, 1947, the housing accommodations located at 430 Daisy Ave., and 537 Melrose Way, Long Beach,

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\* Page numbering appearing at bottom of page of original Reporter's Transcript.

California, have been subject to maximum rents authorized and established pursuant to the Emergency Price Control Act of 1942, as amended. At all times mentioned herein on and after July 1, 1947, said housing accommodations have been subject to maximum rents authorized and in effect pursuant to said Housing and Rent Act of 1947, as amended. At all times mentioned in this complaint said premises have been within the Los Angeles Defense Rental Area.

#### IV.

That the defendants Doe I to Doe X are the fictitious names of the defendants whose true names are to this plaintiff unknown, and plaintiff asks that when these true names are discovered this complaint may be amended by inserting such true names in the place and stead of such fictitious names. Wherever the word "defendant" is used in this complaint, it shall include all of the defendants individually and collectively herein sued.

#### V.

Defendant received from persons for the use and occupancy of said accommodations rents in excess of the maximum rents established pursuant to said Acts. A Schedule is attached hereto and by reference made a part hereof, as though fully set out herein. Said Schedule states the names of the persons using and occupying said accommodations, and the period of occupancy by such persons. Said Schedule states the rents charged to and received from said persons for such use and occupancy during said period. Said

Schedule states the applicable maximum rent. Said Schedule states the amount of the overcharges.

## VI.

In the judgment of the Housing Expediter the defendant has engaged and is about to engage in acts and practices which constitute and will constitute violations of provisions of said Acts and of regulations, orders [3] and requirements issued thereunder.

Wherefore, the plaintiff demands:

A. Judgment for the plaintiff to recover of the defendant treble the total amounts charged to persons, or demanded, accepted or received by the defendant from persons as rent for the use and occupancy of the housing accommodations described in this complaint, within one year prior to the filing of this complaint, which were in excess of the maximum rents established pursuant to said Housing and Rent Act of 1947, as amended, and further that:

B. The defendant be ordered and directed to pay to the Treasurer of the United States for and on behalf of all persons entitled thereto a refund of all amounts in excess of the maximum rents established pursuant to said Acts which were received by the defendant, his agents or employees since the date maximum rents were established for said housing accommodations pursuant to said Acts; provided that refunds made by the defendant for and on be-



half of such persons in compliance with the direction of the Court for rents received within one year prior to the bringing of this action, shall be deducted from the amount of the judgment prayed for in the preceding Paragraph "A"; or, in the alternative, that the defendant be ordered and directed to pay the amount of the overcharge referred to in this Paragraph "B" to the United States of America, and

C. A preliminary and final injunction enjoining the defendant, his agents, servants, employees, and all persons in active concert or participation with him, from:

1. Directly or indirectly charging, demanding, accepting or receiving amounts in excess of the maximum rent established pursuant to the aforesaid Acts, and said Acts as hereafter amended or superseded and the regulations issued thereunder.

2. Directly or indirectly discontinuing, withholding, suspending or shutting off the supply of services, including utilities, heat, hot and cold [4] water, janitorial and maid service, furniture, furnishings, equipment, living space and all other services which the landlord is required to provide by said Acts and the regulations issued pursuant thereto, or threatening to do any of the foregoing with reference to the above described housing accommodations or any other controlled housing accommodations owned, managed or controlled by defendant.

3. Engaging in any action or course of action the purpose of which is to evict illegally tenants from the above-described premises, or any other housing accommodations owned, controlled or managed by the defendant, and from evicting said tenants in any form or manner contrary to said Housing and Rent Act of 1947, as amended, and regulations issued pursuant thereto as heretofore or hereafter amended or superseded.

4. Violating said Housing and Rent Act of 1947, as amended, and any of the regulations issued pursuant thereto, as heretofore or hereafter amended or superseded.

/s/ ASHER SCHEIR,

Attorney, Office of the  
Housing Expediter. [5]

Housing Accommodations Located at 430 Daisy Ave. and  
537 Melrose Way, Long Beach, California

Unit	Name of Tenant	Period of Overcharges	Amount Rent Paid	Maximum Rent	Amount of Overcharges
537	Lily Dolci	11- 5-47 to 12- 5-47	\$30.00 mo.	\$29.00 mo.	\$ 1.00
	(Gutierrez)	12- 5-47 to 1- 5-48	35.00	29.00	6.00
430	A. J. Lynch	6-11-48 to 7-10-48	100.00 mo.	37.50 mo.	62.50
		Cleaning Deposit (\$25.00)			
		7-11-48 to 6-11-49	75.00 mo.	37.50 mo.	412.50
Total amount of overcharges .....					\$482.00

Schedule referred to in Paragraph V of Plaintiff's first cause of action.

[Endorsed]: Filed July 15, 1949. [6]

[Title of District Court and Cause.]

No. 9996-HW

ANSWER TO COMPLAINT FOR TREBLE  
DAMAGES, RESTITUTION AND INJUNC-  
TION

Comes Now the Defendant, Dorothy Sharp, and appearing for herself alone and no other defendant, denies and alleges as follows, to wit:

I.

Answering paragraph V of plaintiff's complaint, this answering defendant denies generally and specifically each and every allegation in said complaint contained, the same as though each of said allegations therein contained were herein set out and specifically denied and particularly, this answering defendant denies that Lilly Dolci paid an overcharge of One (\$1.00) Dollar in rent as alleged in the schedule attached to said complaint and particularly alleges that the One (\$1.00) Dollar alleged to be an overcharge was the amount paid for an extra bed by the said Lilly Dolci, and particularly alleges that there was no overcharge in the Gutierrez matter amounting to Six (\$6.00) Dollars a month, or any other amount, and particularly denies that there was an overcharge of Sixty-two Dollars and fifty cents (\$62.50) a month in the A. J. Lynch matter, or any other sum, or sums, and particularly denies that there was any overcharge of Four Hundred

Twelve Dollars and Fifty Cents (\$412.50) on the A. J. Lynch matter, or any overcharge in any amount whatsoever; [7] and particularly alleges that any aparent overcharge is the direct result of the unlawful conduct of employees of the Office of Housing Expediter in Long Beach, California.

## II.

Answering Paragraph VI of plaintiff's complaint, this answering defendant denies generally and specifically each and every allegation in said paragraph VI contained, the same as though each of said allegations had herein been set out and specifically denied.

And as a Further, Separate, Affirmative and Second Defense Hereto, This Answering Defendant Alleges:

## I.

That the complaint in this matter was filed on or about the 9th day of August, 1949; that the Housing Act provides that no recovery can be made or can a cause of action be maintained for rents alleged to have been over the ceiling price for more than one year prior to the filing of the complaint in this matter, and therefore, any attempt in said complaint to obtain redress for more than one year prior to August 9th, 1949, are barred by the provisions of said Act.

And as a Further, Separate, Affirmative and Third



Defense Hereto, This Answering Defendant Alleges:

I.

That prior to the 11th of June, 1948, the ceiling price upon the accommodations herein sued upon was Ninety (\$90.00) Dollars per month; that thereafter on the 11th day of June, 1948, the defendant in this action entered into a lease with Mr. and Mrs. A. J. Lynch, wherein the defendant herein agreed to lease all the rooms in said housing accommodations to the said Lynch for Seventy-five (\$75.00) Dollars per month, which was fifteen (\$15.00) Dollars under the ceiling in force at said time; that thereafter on or about the 10th day of August, 1948, the employees of the Housing Expediter called this answering defendant into their office and in the presence of witnesses the said employees of the said Housing Expediter by threat and intimidations made in the presence [8] of witnesses did compel this defendant to sign a new rent schedule which reduced the ceiling rents to less than the amount in force and effect upon the date said lease was executed. The said conduct on the part of said employees of the said Husing Expediter was unlawful and in violation of the laws and statutes of the United States of America and were made and done by said employees for the purpose of embarrassing and taking advantage of this defendant and amounted to coercion in forcing this defendant to sign papers which she should not have been made to sign.



Wherefore, this answering defendant prays that plaintiff take nothing by its said cause of action and that she go hence with her costs herein expended.

MATOT, GABRIELSON &  
MANLEY,

By /s/ KENNETH E. MATOT,  
Attorneys for Defendant,  
Dorothy Sharp.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed January 4, 1950. [9]

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[Title of District Court and Cause.]

PLAINTIFF'S REQUEST FOR ADMISSIONS  
UNDER RULE 36

Plaintiff requests the defendant Dorothy Sharp, within ten days after service of this request, to make the following admissions for the purpose of this action only and subject to all pertinent objections to admissibility which may be interposed at the trial:

1. That for all times pertinent to this suit, the defendant Dorothy Sharp was the landlord of the housing accommodations located at 537 Melrose Way and 430 Daisy Avenue, Long Beach, California.

2. That Lily Dolci, now known as Lily Dolci Gutierrez, occupied the housing accommodations

located at 537 Melrose Way from November 5, 1947, to January 5, 1948.

3. That said defendant Dorothy Sharp received from said Lily Dolci, now known as Lily Dolci Gutierrez, the sum of \$30.00 as rent for the use and occupancy of the housing accommodations located at 537 Melrose Way, for the [11] period commencing November 5, 1947, to December 5, 1947.

4. That said defendant Dorothy Sharp received from said Lily Dolci, now known as Lily Dolci Gutierrez, the sum of \$35.00 as rent for the use and occupancy of the housing accommodations located at 537 Melrose Way for the period December 5, 1947, to January 5, 1948.

5. That on or about March 13, 1947, the Area Rent Director for the Los Angeles Defense Rental Area issued an order adjusting maximum rent, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 1.

6. That said order, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 1, is genuine.

7. That said order, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 1, is a part of the official records of the Office of the Housing Expediter.

8. That said order, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 1, established the maximum rent for said housing accom-

modations located at 537 Melrose Way for all times pertinent to this suit.

9. That for all times pertinent to this suit, the maximum rent for said housing accommodations located at 537 Melrose Way, Long Beach, California, was the sum of \$29.00 per month.

10. That A. J. Lynch and family occupied the housing accommodations located at 430 Daisy Avenue, Long Beach, California, from June 11, 1948, to June 11, 1949.

11. That no person or persons other than members of the family of A. J. Lynch occupied said housing accommodations located at 430 Daisy Avenue during the period June 11, 1948, to June 11, 1949.

12. That said defendant Dorothy Sharp received from said A. J. Lynch the sum of \$100.00 as rent for said housing accommodations located at 430 Daisy Avenue for the period June 11, 1948, to July 10, 1948.

13. That \$25.00 of said sum of \$100.00 received by the defendant Dorothy Sharp for the period June 11, 1948, to July 10, 1948, was received as a cleaning deposit.

14. That no part of said cleaning deposit of \$25.00 has been refunded [12] by the defendant Dorothy Sharp to said tenant A. J. Lynch or anyone representing said A. J. Lynch.

15. That said defendant Dorothy Sharp received from said A. J. Lynch the sum of \$75.00 per month

each month as rent for said housing accommodations located at 430 Daisy Avenue for the period July 11, 1948, to June 11, 1949.

16. That on or about January 14, 1949, said Dorothy Sharp filed a registration statement with the Office of the Housing Expediter Area Rent Office, Los Angeles Defense Rental Area, affecting the housing accommodations located at 430 Daisy Avenue, Long Beach, California, a true copy of which registration statement is hereto attached marked Plaintiff's Exhibit No. 2.

17. That said registration statement, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 2, is genuine.

18. That said registration statement, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 2, is a part of the official records of the Office of the Housing Expediter.

19. That the signature appearing on said registration statement, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 2, is the signature of the defendant Dorothy Sharp.

20. That said signature appearing on the registration statement, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 2, was affixed thereto by the defendant Dorothy Sharp.

21. That on or about March 23, 1949, the Area Rent Director for the Los Angeles Defense Rental Area issued an order affecting the housing accommodations located at 430 Daisy Avenue, Long Beach,



California, Decreasing Maximum Rent Requiring Refund to Tenant. A true copy of said order is hereto attached marked Plaintiff's Exhibit No. 3.

22. That said order, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 3, is genuine.

23. That said order, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 3, is a part of the official records of the Office of the Housing Expediter. [13]

24. That said order, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 3, established the maximum rent for all times pertinent to this suit for the housing accommodations located at 430 Daisy Avenue, Long Beach, California.

25. That no appeal has been taken, pursuant to the Procedural Regulations issued pursuant to the Housing and Rent Act of 1947, as amended, by the defendant Dorothy Sharp from said order, a true copy of which is hereto attached marked Plaintiff's Exhibit No. 3.

26. That no part of the monies received by the defendant Dorothy Sharp from Lily Dolci, now known as Lily Dolci Gutierrez, has been refunded by said defendant Dorothy Sharp to said tenant.

27. That no part of the monies received by the defendant Dorothy Sharp from said A. J. Lynch has been refunded to said A. J. Lynch pursuant to the order of the Area Rent Director issued March 23, 1949, a true copy of which is hereto attached



marked Plaintiff's Exhibit No. 3.

28. That no civil action has been filed by said tenants or either of them against said defendant Dorothy Sharp on account of any of the matters alleged above.

Pursuant to Rule 36 of the Federal Rules of Civil Procedure, each of the above matters shall be deemed admitted unless within ten days of the service of this request, the defendant serves upon the plaintiff the sworn statement or written objections described in said Rule 36 of the Federal Rules of Civil Procedure.

Dated: Los Angeles, California, this 13th day of January, 1950.

ABE I. LEVY,

By /s/ ASHER SCHEIR,

Attorney, United States of  
America.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed January 16, 1950. [14]

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[Title of District Court and Cause.]

DEFENDANT'S ANSWER TO PLAINTIFF'S  
REQUEST FOR ADMISSION UNDER  
RULE 36

State of California,

County of Los Angeles—ss.

Comes now the defendant Dorothy Sharp, in answer to plaintiff's request for admissions under Rule 36 and being first duly sworn, deposes and admits, denies and alleges as follows, to wit:

1. Admits the allegations as contained in specification #1 of plaintiff's request.

2. Admits the allegations contained in specification #2 of plaintiff's request.

3. Denies generally and specifically every allegation contained in paragraph 3 of plaintiff's request. Alleges the fact to be that the defendant only received the sum of \$29.00 as rent for said premises from Lily Dolci. [18]

4. Denies generally and specifically each and every allegation contained in plaintiff's specification #4. Alleges the fact to be that the amount received by the defendant was the maximum amount collectable.

5. Answering paragraphs 5, 6 and 7 of plaintiff's request for admission, this answering defendant has no knowledge, information or belief sufficient to enable her denial on such lack of information or belief she denies each and every allegation therein contained.

6. Answering specification #8 of plaintiff's request for admission, this answering defendant has no knowledge, information or belief sufficient to enable her to answer such allegation and basing her

denial on such lack of information or belief, she denies each and every allegation therein contained.

7. Denies generally and specifically all the allegations contained in specification #9 of plaintiff's request for admissions alleges the fact to be that on the 11th day of June, 1948, the ceiling rent on the premises located 537 Melrose Way, Long Beach, California, was the sum of \$95.00 per month.

8. Admits the allegations contained in specification #10 of plaintiff's request for admission.

9. Denies generally and specifically each and every allegation contained in Paragraph 11 of plaintiff's request for admission, alleges the fact to be which was well known to plaintiff or it's employees or agents and particularly the offices of housing expediter that said premises were occupied by three to nine persons other than that of A. J. Lynch and his wife and that said premises during most of the period alleged was occupied by three to nine persons and not 2.

10. Denies generally and specifically each and every allegation [19] contained in specification #12 of plaintiff's request for admissions, alleges the fact to be that the sum of \$75.00 was the amount received as rent for said premises.

11. Admits the allegation contained in specification #13 of plaintiff's request for admissions.

12. Answering the specification #14 of plaintiff's request for admission and alleges the fact to

be the defendant was under no obligations to return cleaning deposit if the amount was used in cleaning the premises after the Lynches vacated.

13. Admits the allegations of specification of plaintiff's request for admission and alleges that on the 11th day of July, 1948, the maximum rent on said premises was the sum of \$95.00 per month.

14. Answering plaintiff's specification #16 of his request for admissions, this answering defendant denies generally and specifically each and every allegation therein contained, alleges the fact to be that an officer or employee of the office of housing expediter and in violation of his oath of office, wrote out in his handwriting all the letters and figures and did practice and commit duress upon the person of the defendant and in the presence of a witness, did compel the defendant under duress to sign the document, set out as Exhibit #2 and that said document by reason thereof is null and void and of no more effect than if it had been forged.

15. Answering specification #17 of plaintiff's request for admission this answering defendant denies that said document is genuine.

16. Answering plaintiff's specifications #18, 19 and 20, this answering defendant refers to statement given in answer to specification #16 and makes such statement in this answer the same as though it had herein been set out.

17. Answering specifications #21, 22, 23 and 24 of plaintiff's request for admissions and alleges that said order was [20] predicated on the registra-



tion statement, referred to its specification #16 of plaintiff's request for admissions which was alleged to have been obtained by an officer of the housing expediter under duress and therefor void and that any order based on such a document is also void and of no force or effect.

18. This answering defendant has no knowledge, information or belief sufficient to enable her to answer specification #28 of plaintiff's request for admissions and therefor basing her denial on such lack of information or belief. She denies each and every allegation contained in said specification #28.

Dated: Los Angeles, California, this 24th day of January, 1950.

/s/ DOROTHY SHARP.

Subscribed and sworn to before me this 24th day of January, 1950.

[Seal]      /s/ THEODORE R. GABRIELSON,  
Notary Public in and for the County of Los Angeles, State of California.

My Commission Expires November 2, 1952.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed January 25. 1950 [21]



[Title of District Court and Cause.]

MEMORANDUM OF OPINION AND  
JUDGMENT ORDER

Westover, J.:

This is an action instituted under the Emergency Price Control Act of 1942, as amended, and the Housing and Rent Act of 1947, as amended.

Defendant Dorothy Sharp was the owner of a duplex in Long Beach, California. She lived in one side of the duplex and rented the other. The rented portion was, on August 14, 1946, registered with the Rent Control Board as a rooming house of three, individual, furnished rooms. They were rented or leased to various individuals, according to the ceiling established, up to June 11, 1948, at which time the defendant made a lease with Mr. and Mrs. [23] A. J. Lynch, leasing the rented part of the duplex "as described in O. P. A. as lower room, upper room, upper middle and upper rear, including kitchen and bath" for \$75.00 per month. The ceiling on the individual rooms of the premises amounted to a total of approximately \$90.00 per month.

Sometime later the Office of Price Administration discovered that all the rooms had been leased to one tenant (Mr. and Mrs. A. J. Lynch) and demanded that the landlord file a new dwelling registration, which was filed on January 14, 1949, and which set forth that the maximum rent as of June 11, 1948 (the date of the lease) was \$75.00 per month. On March 23, 1949, the Office of the Housing Expediter made an order decreasing the rent

from \$75.00 per month to \$37.50 per month, effective June 11, 1948, which order in part provided that the excess collected should be refunded to the tenant within thirty days from the date of the order. Defendant did not make the refund, and plaintiff instituted this action to recover.

The original registration showed the premises registered were "a residence." The premises in question up to June 11, 1948, had never been rented or registered as a furnished apartment.

Section 840.7 of the rent regulations provides in part as follows:

"In any case where the Rent Area Director . . . deems it necessary or appropriate to enter an order on his own initiative he shall, before taking such action, serve a notice on the landlord of the housing accommodations [24] involved, stating the proposed action and the grounds therefor."

There is nothing in the case at bar to indicate the Area Rent Director attempted to follow the directive. The premises in question had been registered as individual, furnished rooms. It was the contention of the Area Rent Control Office that the premises were rented to the Lynches not as individual rooms, but as an apartment and, consequently, a new registration was required. No notice was served upon the defendant stating the proposed action or the grounds therefor. As far as the evidence in this case shows, the order as made on March 23, 1949, reducing the rent from \$75.00 to \$37.50

per month was made upon the initiative of the Housing Expediter, and no reasons were given the landlord for the proposed change. It is assumed that the rent was fixed in accordance with prevailing rents for like accommodations, but there is nothing in the record to indicate in any way that any attempt was made to inform the landlord of the proposed order or the reasons for it.

There is no question but the premises were controlled housing accommodations, inasmuch as the rooms in question had been registered as "rooms."

Section 825.1 provides, in part:

"Rooming house means . . . a building or portion of a building other than a hotel or motor court in which a furnished room or rooms not constituting an apartment are rented on a short-time basis of daily, weekly, or monthly occupancy to more than two paying tenants not [25] members of the landlord's immediate family."

The registration as a rooming house was, at all times mentioned in the complaint, still a valid registration and was never modified in any way. There is no doubt that the Office of the Housing Expediter could have modified the rooming house registration.

The registration made on January 14, 1949, was a new registration and not a modification of the previous one. The only question in this case is whether or not the Office of the Housing Expediter had a right to demand a new registration when the rooms in question were leased to one individual.

Section 825.7 of the Controlled Housing Regulation, issued pursuant to the Housing and Rent Act of 1947, provided that every landlord of controlled housing accommodations rented, or offered for rent, must file a registration statement with the Office of the Housing Expediter for such housing accommodations within thirty days after the first renting.

The requirement of the Rent Control Act to register was originally met by the defendant because, on August 14, 1946, she had filed a registration with the Office of the Housing Expediter and had had the ceiling established on the rooms in the house. Plaintiff now contends that Section 825.7 requires a new registration, as the single rooms were combined and rented as an apartment.

Section 203(a) of the Housing and Rent Act of 1947, as amended, provides:

“After the effective date of this Act, no maximum rents shall be established or maintained under the authority of the [26] Emergency Price Control Act of 1942, as amended, with respect to any housing.”

Plaintiff has been unable to cite any case sustaining its contention but argues that inasmuch as this is the first time the rooms were rented as an apartment, a new registration had to be filed with the Office of the Housing Expediter.

We are not convinced that this is the law under the Housing and Rent Act of 1947, as amended; as the burden of proof is on the plaintiff, we feel



the burden of proof has not been sustained as required and, consequently, that the Office of the Housing Expediter had no authority to require the registration demanded of defendant and no authority to make the order reducing the rent from \$75.00 to \$37.50.

In regard to Unit 537, rented to Lily Dolci, on which plaintiff claims an overcharge of \$1.00 from 11/5/47 to 12/5/47 and \$6.00 from 12/5/47 to 1/5/48, the receipts introduced in evidence given by the defendant Dorothy Sharp indicate that the one dollar was for rent of an additional bed, and the five dollars was cleaning charge for the apartment. There is nothing in the case to indicate that the tenant was entitled to an additional bed without paying therefor nor was entitled to the cleaning of her apartment free of charge; consequently the court is of the opinion that there is no overcharge as to Unit 537.

Judgment for defendant.

[Endorsed]: Filed March 16, 1950. [27]

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[Title of District Court and Cause.]

AMENDED FINDINGS OF FACT AND  
CONCLUSIONS OF LAW

The above-entitled matter came on regularly to be heard on the 24th day of February, 1950, before the Honorable Harry C. Westover, Judge presiding,



in Courtroom No. 5 of the above-entitled Court, the plaintiff appearing by and through Asher Scheir, an attorney for the Office of the Housing Expediter, and the defendant, Dorothy Sharp, appearing by and through Matot, Gabrielson & Manley, by Kenneth E. Matot, her attorneys; hearing by jury having been waived by both the plaintiff and defendant, and evidence, both oral and documentary, having been introduced, and the case closed, the Court, being fully informed in the premises, now makes its Findings of Fact and Conclusions of Law as follows, to wit:

### Findings of Facts

#### I.

It is true that at all times mentioned herein prior to July [29] 1, 1947 the housing accommodations located at 430 Daisy Avenue and 537 Melrose Way, Long Beach, California, have been subject to a maximum rent authorized and established pursuant to the Emergency Price Control Act of 1942, as amended. That at all times mentioned herein on and after July 1, 1947, said housing accommodations have been subject to a maximum rent authorized and in effect pursuant to said Housing and Rent Act of 1947, as amended; that at all times mentioned in the complaint said premises have been within the Los Angeles Defense Rental Area.

#### II.

It is not true that the defendant, Dorothy Sharp, received from persons for the use and occupancy of

said accommodations, rent in excess of the maximum rent established pursuant to said Act. It is true that said schedule as set out in plaintiff's complaint and made a part hereof by reference, states the rent charged to and received from said persons for such use and occupancy during said period. It is not true that said schedule states the applicable maximum rent. It is not true that said schedule states the amount of the overcharges.

### III.

It is not true that the defendant charged Lily Dolci \$1.00 or any other sum or sums in excess of the maximum rent on said premises occupied by said Lily Dolci.

### IV.

It is not true that the defendant overcharged A. J. Lynch the sum of \$37.50 per month from the 11th day of June, 1948, to the 10th day of July, 1948, or that there was an overcharge of \$62.50 for said time, or any other sum or sums whatsoever.

### V.

It is not true that the defendant overcharged A. J. Lynch for the period from July 11, 1948, to June 11, 1949, in the sum of \$37.50 per month, or amounting to the sum of \$412.50, or any other [30] sum or sums.

### VI.

It is true that all amounts charged the defendant, A. J. Lynch, for the months beginning on the 11th day of July, 1948, to the 11th day of June, 1949,

were less than the maximum ceiling established for said premises.

## VII.

It is true that that portion of the premises described in plaintiff's complaint herein, namely, 430 Daisy Avenue, Long Beach, California, was duly registered with the Rent Control Board on the 14th day of August, 1946 as a rooming house, of four individual furnished rooms. It is true that the total ceiling rent on said premises under said registration was the sum of approximately \$90.00 per month.

## VIII.

It is true that on or about the 11th day of June, 1948, the defendant herein entered into a written lease with the said Mr. and Mrs. A. J. Lynch, and that by virtue of the terms thereof the said defendant rented said premises as described in said lease to the said Mr. and Mrs. A. J. Lynch at \$75.00 per month for said term.

## IX.

It is true that the premises in question up to June 11, 1948, had never been rented or registered as a furnished apartment.

## X.

It is true that the Rent Director has never attempted to change or modify the registration of August 14, 1946.

## XI.

It is true that the order by the Rent Director as

made on March 23, 1949, reducing the rent from \$75.00 to \$37.50 per month, was made on the initiative of the Housing Expediter, and that no reasons were given the landlord for the proposed [31] change, as required by law.

## XII.

It is true that the registration on August 14, 1946 of said accommodations at all times mentioned in the complaint is still a valid registration and was never modified in any way.

## XIII.

It is true that the registration made on January 14, 1949 was a new registration and not a modification of the previous one.

## XIV

It is true that the defendants in said action originally registered said accommodations within thirty days after first originally renting the same.

## XV.

That the entire housing accommodations located at 430 Daisy Avenue, Long Beach, California, consisted of the following: rear room, upper room, upper middle and upper rear, including kitchen and bath.

## XVI.

That the entire unit designated as 430 Daisy Avenue, Long Beach, California, was rented to Mr. and Mrs. A. J. Lynch.

## XVII.

That during the tenancy of Mr. and Mrs. A. J.



Lynch, no part of the housing accommodations located at 430 Daisy Avenue, Long Beach, California, was rented to anyone other than Mr. and Mrs. A. J. Lynch.

XVIII.

That the A. J. Lynch family consisted of Mr. A. J. Lynch, Mrs. A. J. Lynch, and one child.

XIX.

That the entire unit at 430 Daisy Avenue, Long Beach, California, was rented for the first time in its entirety on June 11, 1948, to said Mr. and Mrs. A. J. Lynch. [32]

XX.

That the Memorandum of Opinion and Judgment Order filed by this Court on the 16th day of March, 1950, is made apart of these Findings, the same as though it had herein been set out and pleaded in full.

Conclusions of Law

From the foregoing Findings of Fact, the Court makes the following Conclusions of Law:

That the plaintiff, United States of America, is not entitled to judgment against the defendant, Dorothy Sharp, and that the said defendant is entitled to judgment against the plaintiff.

Let judgment be entered accordingly.

Done in open Court this 10th day of May, 1950.

/s/ HARRY C. WESTOVER,  
Judge.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed May 10, 1950. [33]



In the United States District Court, Southern  
District of California, Central Division

No. 9996-HW

UNITED STATES OF AMERICA,

Plaintiff,

vs.

DOROTHY SHARP, DOES I TO X,

Defendants.

### JUDGMENT

The above-entitled matter came on regularly to be heard on the 24th day of February, 1950, before this Honorable Court, in courtroom No. 5 thereof, the Honorable Harry C. Westover, Judge presiding, a jury having been waived by both parties, and evidence both oral and documentary having been introduced, and the Court being fully informed in the premises, and the Court having filed its Findings of Fact and Conclusions of Law, being the decision of this Court.

It Is Accordingly Ordered, Adjudged and Decreed that the plaintiff, United States of America, take nothing by its complaint, and that the defendant, Dorothy Sharp, have judgment against the plaintiff.

Dated this 10th day of May, 1950.

/s/ HARRY C. WESTOVER,  
Judge.

Affidavit of Service by Mail Attached.

Judgment entered May 10, 1950.

[Endorsed]: Filed May 10, 1950. [35]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is Hereby Given that United States of America, plaintiff above named, hereby appeals to the United States Circuit Court of Appeals, for the Ninth Circuit, from the entire final judgment entered in this action on the 10th day of May, 1950.

Dated: Los Angeles, California, this 6th day of July, 1950.

ABE I. LEVY,

ASHER SCHEIR,

By /s/ ASHER SCHEIR,

Attorneys for Appellant,  
United States of America.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed July 7, 1950. [37]

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In the United States District Court, Southern  
District of California, Central Division

No. 9996-HW

UNITED STATES OF AMERICA,

Plaintiff,

vs.

DOROTHY SHARP, DOES I TO X,

Defendants,

Honorable Harry C. Westover, Judge Presiding.

REPORTER'S TRANSCRIPT OF  
PROCEEDINGS

February 25, 1950

Appearances:

For the Plaintiff:

ABE I. LEVY, ESQ., and

ASHER SCHEIR, ESQ.,

Office of The Housing Expediter.

For the Defendant, Dorothy Sharp:

MATOT, GABRIELSON & MANLEY by:

KENNETH MATOT, ESQ.

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The Clerk: No. 9996-B, United States vs. Dorothy Sharp, Does I to X.

The Court: Call your first witness.

Mr. Matot: If the Court please, because of a situation involved in this case, I think it would be well if counsel made an opening statement, so the Court would know what the situation is that we have here. This is not an ordinary overcharge matter.

Mr. Scheir: Your Honor, I cannot agree with counsel.

The Court: I don't know why there is any necessity to waste time on an opening statement. I will get the facts as we go along.

Mr. Matot: I make a motion at this time, under

the provisions of Section 205 of the Housing and Rent Act of 1947, which amends Section 204 of the original Act, and ask that all testimony as to overcharge come within one year of the date of the filing of the complaint.

The Court: Well, I think that proposition has been definitely decided by this Court and other Courts. The statute does not run on overcharges; it runs on treble damages. Now, as to treble damages prior to a year, I think they are out, but not as to overcharges, not as to restitution; so your motion will be denied. [2\*]

Mr. Matot: By the way, I would like to inquire if the whole record pertaining to this case is here.

Mr. Scheir: The entire official record pertaining to these premises is here, your Honor.

Mr. Hamlin.

EDWIN D. HAMLIN

called as a witness by and on behalf of the Plaintiff, having been first duly sworn, was examined and testified as follows:

The Clerk: Your name?

The Witness: Edwin D. Hamlin.

Direct Examination

By Mr. Scheir:

Q. Mr. Hamlin, by whom are you employed?

A. The Office of the Housing——

The Court: I think counsel will probably stipulate to his qualifications. Probably counsel knows Mr. Hamlin.

(Testimony of Edwin D. Hamlin.)

Mr. Matot: Yes, no question about it. I know him well.

The Court: All right, counsel will stipulate?

Mr. Matot: Yes.

The Court: Is there any argument about the maximum rent?

Mr. Matot: Yes, there is a very serious argument.

Q. (By Mr. Scheir): Mr. Hamlin, you have the official records here, the records pertaining to 537 Melrose Way,— A. Yes, I do. [3]

Q. —Long Beach, California? A. Yes.

Q. Mr. Hamlin, I show you what purports to be an Order Determining Maximum Rent, affecting the housing accommodations at 537 Melrose Way, Long Beach, California, and ask you if that is part of the official records of the Office of the Housing Expediter? A. Yes, it is.

Mr. Scheir: Your Honor, I offer this Order Determining Maximum Rent for the accommodations located at 537 Melrose Way, which Order was dated August 22, 1944, in evidence as Plaintiff's Exhibit No. 1, and ask leave to withdraw the original and substitute therefor a certified copy.

Mr. Matot: I am going to object to the introduction of that document, upon the ground and for the reason that that Order was modified by Order of—

The Court: Mr. Matot, you may introduce all the modifications you want to. This is the original order. It is my policy in these rent cases to be



(Testimony of Edwin D. Hamlin.)

very liberal relative to the introduction of evidence, and overrule practically all objections. I try to get all the facts before the Court.

Mr. Matot: But the trouble is that was on another part of the same building, at the time that order was made. For that reason I object to it on the ground it doesn't involve [4] these accommodations, but involves other accommodations.

The Court: Overruled.

(The document referred to was marked "U. S. Exhibit No. 1," and was received in evidence.)

U. S. A. EXHIBIT No. 1

OPA

Form D-41

Stamp of Issuing Office.

Office of Price Administration

Rent Division

233 East Broadway

Long Beach 2, California

United States of America

Office of Price Administration

ORDER DETERMINING MAXIMUM RENT

Concerning (Description of Accommodations) 537  
Melrose Way, Long Beach, California.

Docket No. 25089-A.

(Testimony of Edwin D. Hamlin.)

To (Name and Address of Landlord):

Mrs. Dorothy Sharp,  
430 Daisy Avenue,  
Long Beach, California.

(Copy)

The Rent Director has duly considered the above matter and:

☐ Finds that the rent on the Maximum Rent Date was \$. . . . . per which amount is the Maximum Rent for the above-described accommodations.

☒ The Maximum Rent for the above-described accommodations is hereby fixed at \$25.00 per month the rent which the Rent Director finds was the rent generally prevailing in this Defense-Rental Area for comparable housing accommodations on the maximum Rent Date (Furnished).

Without electric services, but including gas and heat for cooking, and water.

Issued August 22, 1944.

/s/ DAVID BARRY, JR.,

Rent Director.

Copy to (Name and Address of Tenant): Tenant-Occupant, 537 Melrose Way, Long Beach, California.

I certify this is a true and correct copy of the order issued under Docket No. 25089-A issued by the Long Beach area office of the Office of the Housing Expediter.

/s/ ALICE WEAVER,

Dkt. Clerk.

[Endorsed]: Filed August 4, 1950.

(Testimony of Edwin D. Hamlin.)

Q. (By Mr. Scheir): Mr. Hamlin, I show you an Order Adjusting Maximum Rent, issued March 13, 1947, affecting housing accommodations at 537 Melrose Way, Long Beach, California, and ask you if that is part of the official records of the Office of the Housing Expediter.

A. Yes, it is.

Mr. Matot: And the same objection to this.

The Court: Same objection, and same ruling.

Mr. Scheir: I offer this in evidence, your Honor, as Plaintiff's Exhibit No. 2, and ask leave to withdraw the original and substitute therefor a photostatic copy.

The Court: It may be admitted.

(The document referred to was marked "U. S. Exhibit No. 2," and was received in evidence.)

U. S. EXHIBIT No. 2

United States of America

Office of Temporary Controls

Office of Price Administration

Office of Temporary Controls, Office of Price Administration, Rent Division, Long Beach Defense Rental Area, 110 East Anaheim, Long Beach, California.

Concerning (address of accommodations): 537 Melrose Way, Long Beach, California.

Docket No. 92450 RJA:k.

(Testimony of Edwin D. Hamlin.)

To (Name and Address of Landlord): Mrs. Dorothy Sharp, 428 Daisy Avenue, Long Beach, California.

To (Name and Address of Tenant): Tenant-Occupant, 537 Melrose Way, Long Beach, California.

The Rent Director, after consideration of all the evidence in this matter, has determined that the Maximum Rent for the above-described accommodations should be adjusted on the grounds stated in Section(s) 5(a)(3) of the Rent Regulation.

For added dishes, silver and cooking utensils and services of all electricity.

Therefore, it is ordered that the Maximum Rent for the above-described housing accommodations be, and it hereby is, changed from \$25.00 per month to \$29.00 per month.

Issued March 13, 1947, and effective March 13, 1947. This order is now in effect and will remain in effect until changed by the Office of Price Administration. Consideration given but no adjustment allowed on other grounds given by landlord in petition.

/s/ B. C. KOEPKE,

Area Rent Director for Los Angeles Defense Rental Area.

Admitted Feb. 24, 1950.

(Testimony of Edwin D. Hamlin.)

Q. (By Mr. Scheir): Mr. Hamlin, do you have the official records of the Office of the Housing Expediter pertaining to the accommodations located at 430 Daisy Avenue, Long Beach?

A. Yes, I do.

Q. Mr. Hamlin, I show you what purports to be a registration statement affecting the accommodations at 430 Daisy Avenue, Long Beach, California, received January 14, [5] 1949, and ask if that is part of the official records of the Office of the Housing Expediter.

A. Yes.

Mr. Matot: Now, your Honor, we are going to object to that on the ground that the government filed a Request for Admission, and Rule 36 requires us to answer, and that becomes a part of the pleadings before this Court. Now, in that pleading we allege and set out that this document was secured under duress, and we will prove that by direct proof.

The Court: Overruled. You will have a chance to prove that when your time comes.

Mr. Scheir: If the Court please, I offer in evidence the statement affecting the housing accommodation 430 Daisy Avenue, bearing "Received" stamp of January 14, 1949, and ask leave to withdraw the original and substitute therefor a certified copy.

The Court: It may be received.

Mr. Matot: We object to it, your Honor.

The Court: Same ruling.

Mr. Scheir: Your Honor, inasmuch as the validity of the Registration statement seems to be in



(Testimony of Edwin D. Hamlin.)

issue, may I withdraw the original at the conclusion of the trial?

The Court: You may.

The Clerk: No. 3.

(The document referred to was marked "U. S. Exhibit No. 3," and was received in evidence.) [6]

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#3

## GENERAL INSTRUCTIONS

The landlord is required to register separately each rental dwelling unit, whether occupied or vacant. A dwelling unit is a room or a group of rooms for which a single rent is paid. Complete a Registration Statement in triplicate. (If not typewritten, be sure ink pressure is used so that both carbon copies are clear and distinct.)

move carbons, and mail or bring the three copies to the Area Rent Office.

extra sheets, in triplicate, for sections "D" & "E" if necessary.

Effective Date

# UNITED STATES OF AMERICA

## OFFICE OF PRICE ADMINISTRATION

### REGISTRATION OF RENTAL DWELLINGS

(TYPE OR PRINT PLAINLY-DO NOT FOLD)

(Do Not Use This Form for Hotels and Rooming Houses)

Form Approved by  
Service No. 08-8079-1  
Form DD-U

AREA OFFICE  
COPY

## IDENTIFICATION

1. 430 Daisy Ave  
Address of the rental dwelling unit
2. \_\_\_\_\_  
Apartment number or location
3. Number of Rooms in unit being registered. 5
4. Total Number of dwelling units in this structure. 2

## SECTION A. MAILING ADDRESS OF LANDLORD

Name of Landlord Dorothy Sharp

Name of Agent \_\_\_\_\_

Address Mail to: Dorothy Sharp

## SECTION B. MAILING ADDRESS OF TENANT

Name of Tenant A. J. Lynch

Address 430 Daisy Ave

City and State Long Beach, Calif.

## SECTION C. MAXIMUM RENT

Read carefully and fill in every item which applies to this dwelling unit.

Rent on "Maximum Rent date" \$ \_\_\_\_\_ per week ( ) per month ( )

Not rented on "Maximum Rent date" but rented at any time during the two-month period ending on "Maximum Rent date".

Date last rented during that two-month period: \_\_\_\_\_ 194 \_\_\_\_\_

Rent on that date: \$ \_\_\_\_\_ per week ( ) per month ( )

Not rented on "Maximum Rent date" nor at any time during the two-month period ending on "Maximum Rent date," but rented after "Maximum Rent date."

Check one box if applicable:

- ☐ (a) Owner occupied or vacant on "Maximum Rent date" and during two-month period ending on "Maximum Rent date".
- ☐ (b) Newly constructed without priority rating.
- ☐ (c) Newly constructed with priority rating. (If checked, item 6 must also be filled in.)

Date first rented after "Maximum Rent date." June 11 194 \_\_\_\_\_

Rent on that date: \$ 75.00 per week ( ) per month ( )

Dwelling unit made available by a change which resulted in an increase or decrease in the number of dwelling units after "Maximum Rent date."

Date first rented after such change: \_\_\_\_\_ 194 \_\_\_\_\_

Rent on that date: \$ \_\_\_\_\_ per week ( ) per month ( )

Substantially changed after "Maximum Rent date," but before the "effective date." Check one if applicable:

- ☐ (a) From unfurnished to fully furnished.
- ☐ (b) From fully furnished to unfurnished.
- ☐ (c) By a major capital improvement AS DISTINGUISHED FROM ORDINARY REPAIR, REPLACEMENT AND MAINTENANCE.

Date first rented after such change: \_\_\_\_\_ 194 \_\_\_\_\_

Rent on that date: \$ \_\_\_\_\_ per week ( ) per month ( )

Dwelling unit newly constructed with a priority rating from the United States or any agency thereof.

Rent approved by agency granting priority: \$ \_\_\_\_\_ per week ( ) per month ( )

## THE MAXIMUM RENT FOR THIS DWELLING UNIT IS:

Enter Maximum Rent in accordance with the following instructions:

1. If only one of the above items applies to this dwelling unit the Maximum Rent is the rent entered for that item.

2. If more than one of the above items apply to this dwelling unit the Maximum Rent is the rent reported for the most recent date, except in the case of Item 6.

3. If item 6 applies to this dwelling unit the Maximum Rent is the lower of the rents entered in 1, 2, or 3.

4. Note: If any one of the items 1b), 4 or 5 applies to this dwelling unit you must also fill in the information on Section C-7. The Rent Director may at any time order a decrease in the Maximum Rent determined under Items 1, 2, 3, 4, or 5, on the ground that the rent is higher than the rent generally prevailing for comparable housing accommodations on the "Maximum Rent date."

Order issued by Rent Director dated \_\_\_\_\_ established maximum rent \_\_\_\_\_ and \_\_\_\_\_ of

\$ \_\_\_\_\_ per week ( ) per month ( )

## Section E. - See Note Section C. 7

If item 3(b), 4 or 5 of Section C was filled in, set forth in spaces the detail the type and cost of:

- (a) New construction (c) A change from unfurnished to fully furnished
- (b) A change in the number of dwelling units (d) A major capital improvement

The unit formerly rented as room

## SECTION D. EQUIPMENT AND SERVICES.

(Check the equipment and services included in the rent on "Maximum Rent date" or the most recent date you entered in Section C.) (ANSWER "YES" or "NO")

## 1. EQUIPMENT

	YES	NO
Furniture	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Running Water	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Hot Water	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Flush Toilet	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Bathroom	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Central Heating	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Heating Stove	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Mech. Refrigerator	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Electricity Installed	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Cooking Stove	<input checked="" type="checkbox"/>	<input type="checkbox"/>

If any equipment is shared, explain below:

## 2. SERVICES

	YES	NO
Garage	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Heat or Heating Fuel	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Cooking Fuel	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Cold Water	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Hot Water	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Light	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Ice or Refrigeration	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Janitor Service	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Garbage Disposal	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Painting & Decorating	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Interior Repairs	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Exterior Repairs	<input type="checkbox"/>	<input checked="" type="checkbox"/>

List any other services:

12.00 per month for hot water

hot water paid by LL & T

Are all equipment and services indicated above now included in the rent? Yes ( ) No ( )

If "No" you must also file Form D-2

## WARNING

The rent for this dwelling unit on and after the "effective date" can be no more than the Maximum Rent entered in Section C, Item 7, unless changed by order of the Rent Director (see Section C, Item 8).

A false statement on this form or an evasion or attempted evasion of the Maximum Rent Regulation may subject you to a \$5,000 fine or imprisonment for one year.

I HEREBY REPRESENT that all statements and entries given herein are true and correct.

(Signature of Landlord or his Agent)

Date 1/18/47



(Testimony of Edwin D. Hamlin.)

Q. (By Mr. Scheir): Mr. Hamlin, I show you what purports to be an Order Decreasing Maximum Rent Requiring Refund to Tenant, affecting housing accommodation 430 Daisy Avenue, Long Beach, California, which order was issued March 23, 1949, and ask if that is part of the official records of the Office of the Housing Expediter.

A. Yes, it is.

Mr. Matot: Now, we object to this document on two grounds: On the first ground, that there is another order which antedates this order and therefore this order may not be introduced until the Government offers the prior order showing that this order modifies the prior order; and upon the further ground that this order was obtained under duress.

The Court: Overruled.

Mr. Scheir: If the Court please, I offer in evidence the Order Decreasing Maximum Rent Requiring Refund to Tenant affecting housing accommodation 430 Daisy Avenue, Long Beach, which order was issued March 23, 1949, as Plaintiff's Exhibit No. 4, and ask leave to withdraw the original and substitute therefor a photostatic copy.

The Court: It may be admitted.

(The document referred to was marked "U. S. Exhibit No. 4," and was received in evidence).

(Testimony of Edwin D. Hamlin.)

U. S. EXHIBIT No. 4

United States of America  
Office of The Housing Expediter  
Office of Rent Control

ORDER DECREASING MAXIMUM RENT  
REQUIRING REFUND TO TENANT

Stamp of Issuing Office: Office of Housing Expediter, 110 East Anaheim, Long Beach 13, California.

Docket No. 99837-RJA-b

Concerning (Address of Accommodations), 430 Daisy Ave., Long Beach, California.

To (Name and address of landlord):

Dorothy Sharp,  
428 Daisy Ave.,  
Long Beach, Calif.

The Rent Director, after consideration of all the evidence in this matter, has determined that the maximum rent for the above-described housing accommodations should be decreased on the grounds stated in Section 5C1 of the Rent Regulation, and further for the reason stated in Section(s) 5C1 of the Rent Regulation, and further for the reason(s) stated in Section(s) 5C1 of the rent regulation, the maximum rent so decreased and determined by this Order shall be effective from 6/11/48.

Therefore, it is ordered that the maximum rent for the above-described accommodations be, and it



(Testimony of Edwin D. Hamlin.)

hereby is, decreased from \$75.00 per month to \$37.50 per month, effective from 6/11/48. No rent in excess of \$37.50 month (maximum rent established by this Order) may be received or demanded.

Any rent collected from the effective date of this Order in excess of the amount provided in this Order shall be refunded to the tenant within 30 days from the date this Order is issued unless the refund is stayed in accordance with the provisions of Rent Procedural Regulation No. 1.

This Order is now in effect and will remain in effect until changed by the Office of the Housing Expediter. Landlord's Letter dated 3/9/49 has been considered.

Issued: March 23, 1949.

/s/ B. C. KOEPKE,

Area Rent Director for Los Angeles Defense Rental Area.

Notice to Landlord and Tenant: Read the reverse side

To (Name and address of tenant):

Tenant Occupant,  
430 Daisy Ave.,  
Long Beach, California.

cc: Compliance.

Admitted: February 24, 1950.

(Testimony of Edwin D. Hamlin.)

Q. By Mr. Scheir: Mr. Hamlin, are there any other orders or documents in the official records affecting the [7] maximum rent for the unit as an entirety at 430 Daisy Avenue, Long Beach, California? A. No, there are not.

Mr. Scheir: I have no further questions.

Cross-Examination

By Mr. Matot:

Q. Mr. Hamlin, have you in your file the order fixing maximum rent on the 20th day of August, 1948?

A. Yes. That applies to rooms within that——

Q. Very well; that is all I asked you. Have you that order? A. Yes.

Q. Have you also the order of June 29, 1948?

A. Yes, I have. That also applies to rooms.

Mr. Matot: I ask leave now to introduce these two orders, your Honor.

The Court: If you will get the orders from Mr. Hamlin——

Q. (By Mr. Matot): Will you give me those orders, please?

A. Have you got copies?

Q. I have got copies.

A. All right; these are the originals. The ones you have appear to be the originals. They must have been issued in duplicate.

Mr. Matot: Well, let me show them to counsel.

Mr. Scheir: Very well, your Honor, I will

(Testimony of Edwin D. Hamlin.)

stipulate [8] these are copies of the originals.

Mr. Matot: May I offer these and ask that they be marked Defendant's Exhibit A?

The Court: They may be admitted.

(The documents referred to were marked, collectively, Defendant's Exhibit A, and received in evidence).

Q. (By Mr. Matot): Now, Mr. Hamlin, will you refer to your records and tell me if this last order—pardon me. Will you tell me if you have in your file any order modifying these two orders, one of 8/20/48 and one of June 29, 1949?

A. As applicable to rooms——

Q. Will you answer my question. Have you any orders modifying those orders?

A. Not as to rooms within——

Mr. Matot: Your Honor, I ask that this witness be instructed to answer the question.

The Court: The answer is "No," Mr. Matot, he hasn't any orders.

Mr. Matot: Very well. I think that is all with this witness.

### Redirect Examination

By Mr Scheir:

Q. Mr. Hamlin, I call your attention to the Registration statement, now in evidence, marked Plaintiff's Exhibit No. 3, and ask you whether that applies to the housing accommodations [9] at 430 Daisy Avenue in their entirety, or whether it applies to individual rooms.

(Testimony of Edwin D. Hamlin.)

Mr. Scheir: I object to that on the ground it is argumentative. The record speaks for itself, your Honor.

The Court: Sustained.

Mr. Scheir: Very well, your Honor. I have no further questions.

(Witness excused.)

Mr. Scheir: I call Mrs. Lynch.

### LAVONNE LYNCH

called as a witness by and on behalf of the Plaintiff, having been first duly sworn, was examined and testified as follows:

The Clerk: Your name, please?

The Witness: Lavonne Lynch.

The Clerk: Take the stand.

### Direct Examination

By Mr. Scheir:

Q. Mrs. Lynch, have you ever lived at 430 Daisy Avenue, Long Beach, California?

A. Yes, sir.

Q. During what period of time did you live there?

A. I lived there from June 15th—16th—June 16th to April 30th.

Q. And will you give us the years, please?

A. The year started—of 1948, I am sorry, to 1949. [10]

Q. And you moved out when?

A. April 30th.

(Testimony of Lavonne Lynch).

Q. Of 1949?           A. Of 1949.

Q. Mrs. Lynch, will you please tell the Court how you learned about the house accommodations at 430 Daisy Avenue?

Mr. Matot: Now, I object to that on the ground that it is incompetent, irrelevant and immaterial.

The Court: How is this material?

Mr. Scheir: It is material, your Honor, inasmuch as the defense seems to be that the Registration statement and the order pertaining to rooms in the structure should apply, whereas the Plaintiff contends the maximum rent for the entire unit should apply.

The Court: Isn't that for the Court to decide?

Mr. Matot: I think——

The Court: Just a minute, Mr. Matot.

Mr. Scheir: It is very material to determine what the rental arrangement was when the tenant rented from the landlord.

The Court: Well, your question is, How did she learn? What does that have to do with it?

Mr. Scheir: Well, it appears, your Honor, that the rental of this unit was advertised in a newspaper——

Mr. Matot: I object to that very [11] strenuously.

The Court: Overruled. She may answer.

Mr. Scheir: Will you answer the question?

The Witness: We found the ad in a newspaper, a Long Beach newspaper, The Independent.



(Testimony of Lavonne Lynch).

Q. By Mr. Scheir: Do you recall the date?

A. June 11, 1948.

Q. Mrs. Lynch, I show you what appears to be a photostatic copy of *The Independent* dated June 11, 1948, and ask if the ad that you saw appears on that photostatic copy.

Mr. Matot: Now, your Honor, I object to that on the ground there is no foundation laid.

The Court: Overruled. She is just asked to look.

The Witness: The ad is present on this paper.

Mr. Scheir: The ad is present on the paper.

Your Honor, at this time I would like to call the representative from the newspaper, inasmuch as she is particularly anxious to get away, and I think this might be an appropriate point to lay the foundation and introduce the copy of the newspaper.

The Court: Any objection?

Mr. Matot: Yes, I object to it as incompetent, irrelevant and immaterial.

The Court: Overruled. You may call her.

Mr. Scheir: Step down, please.

(Witness temporarily excused). [12]

Mr. Scheir: Mrs. Smith.

### LOIS G. SMITH

called as a witness by and on behalf of the Plaintiff, having been first duly sworn, **was examined** and testified as follows:

The Clerk: Your name, please?

The Witness: Lois G. Smith.

(Testimony of Lois G. Smith).

The Clerk: Take the stand, please.

Direct Examination

By Mr. Scheir:

Q. Mrs. Smith, by whom are you employed?

A. Long Beach Independent.

Q. In what capacity?

A. Classified advertising manager.

Q. In your capacity as the advertising manager, do you have access to the official records of that organization? A. Of all records, yes.

Q. Do you have with you today the official newspaper published on June 11, 1948, of The Independent of Long Beach?

A. I do, in the permanent bound form.

Q. Will you turn to that newspaper, please.

(Witness complies with request.)

Q. Mrs. Smith, I show you a photostatic copy of what purports to be a page of the June 11, 1948, issue of The Independent, and ask you if that is a photostatic copy—— A. It is. [13]

Q. ——of page 43 appearing in the newspaper of that date? A. It is.

Q. I call your attention to an ad enclosed in red, appearing on column number 5 of page 43, and ask you if the ad enclosed in red on the photostatic copy appears in the original of your newspaper of that date? A. It does.

Mr. Scheir: Mr. Matot, would you like to see the original of this newspaper?

(Counsel examines document.)

(Testimony of Lois G. Smith).

Mr. Scheir: If the Court please, I would like to introduce a photostatic copy of the original, a photostatic copy bearing the certification of the proper officer of The Independent.

The Court: Any objection?

Mr. Matot: No, I won't object to that.

The Court: It may be received.

The Clerk: No. 5.

(The document referred to was marked "U. S. Exhibit No. 5," and was received in evidence).

Mr. Scheir: I have no further questions.

The Court: Do you want to ask the witness any questions?

Mr. Matot: No, your Honor.

The Court: You may be excused.

(Witness excused.) [14]

Mr. Scheir: If the Court please, I would like to recall Mrs. Lynch now.

### LAVONNE LYNCH

resumed the stand as a witness called by and on behalf of the Plaintiff and, having been previously duly sworn, testified further as follows:

#### Direct Examination

(Continued)

By Mr. Scheir:

Q. Mrs. Lynch, I show you photostatic copy of page 43 of the Long Beach Independent dated June

(Testimony of Lavonne Lynch).

11, 1948, which is now in evidence as Plaintiff's Exhibit No. 5, and ask if the ad that you saw pertaining to the accommodations at 430 Daisy Avenue appears in that photostatic copy?

A. It does appear here.

Q. Would you please read that portion which pertains to the subject premises?

A. "\$75—2 bedroom duplex, close in; Westside. Adults. Lease 1 year. Phone 64-1123."

Q. And that phone number you just read, whose phone number is that?

A. It is Dorothy Sharp's.

Mr. Matot: I move to strike that out as hearsay.

The Court: Overruled.

Q. By Mr. Scheir: Mrs. Lynch, after you read that ad, what did you do? [15]

A. We called that number on the telephone.

Q. And whom did you speak to?

A. We spoke to Mrs. Sharp's daughter, and then we asked if Mrs. Sharp was there—or asked if the lady who was advertising was there, and she said, "No, but she will return in a few moments," and she gave us the address. And we went over, and by that time Mrs. Sharp had returned.

Q. When you say "we," who do you mean?

A. My husband and myself.

Q. Where was Mrs. Sharp living at the time or after you read the ad?      A. 428 Daisy.

Q. Where is 428 Daisy with relation to 430?



(Testimony of Lavonne Lynch).

A. Part of the same duplex, the other side. Part of the same building.

Q. When you visited 428 Daisy Avenue, did you speak to Mrs. Sharp?      A. Yes.

Q. Will you please tell the Court what was said at that time.

A. We asked Mrs. Sharp if the place was yet rented. She said, "No," so we asked if we might see it.

She took us over and showed us the accommodations, and we went over it with her and decided it would be all right, but she could not make up her mind whether or not she wanted [16] to rent it.

Mr. Matot: I object to that "couldn't make up her mind," and move it be stricken.

The Court: It may go out.

Q. (By Mr. Scheir): Did she rent the place to you at that time?      A. No.

Q. Did you see Mrs. Sharp again or speak to her again?      A. We saw her next day.

Q. What happened at that time?

A. She still had not determined whether to rent it to us.

Q. Did you see her after that?

A. Yes, the following day.

Q. What happened at that time?

A. She came over to the motel where we were staying to make inquiry whether or not we would object to her daughter's piano practicing for an hour in the afternoon; and we still didn't know whether we had the place.



(Testimony of Lavonne Lynch).

Q. Mrs. Lynch, did you rent the place at that time?      A. No.

Q. Tell us about the next time you saw or talked to Mrs. Sharp?

A. We went over to see her the next day, and she decided to rent the place to us.

Mr. Matot: I move to strike what she decided to do. [17]

The Court: It may go out.

Q. (By Mr. Scheir): What did she say about renting the place?

A. She said she had decided to rent it to us.

Q. Did she rent it to you at that time?

A. Orally. We did not have leases until the following day.

Q. Mrs. Lynch, I show you what purports to be a lease dated June 11, 1948, for premises known as 430 Daisy Avenue, Long Beach, California, and ask you if that is the lease which you signed at that time.      A. It is.

Mr. Scheir: If the Court please, I offer this lease dated June 11, 1948, in evidence as Plaintiff's Exhibit No. 6.

The Court: It may be received.

(The document referred to was marked "U. S. Exhibit No. 6" and was received in evidence.)

(Testimony of Lavonne Lynch).

U. S. A. EXHIBIT No. 6

Lease

General

This Indenture, Made the Eleventh day of June, 1948, between Dorothy Sharp and Mr. and Mrs. A. J. Lynch. Lessee (whether one or more).

Witnesseth: That the said Lessor has leased, and by these presents does grant, demise and lease unto the said Lessee, and the said Lessee has hired and taken, and by these presents does hire and take of and from the said Lessor,

Premises known as 430 Daisy Ave., Long Beach, Calif. and described in O. P. A. as Lower room—Upper front—Upper middle—Upper rear. Including kitchen and bath. For use of immediate family only under the agreement of this lease.

To include furniture and furnishings as stated in rental agreement inventory.

with the appurtenances, for the term of One Year, commencing on the Eleventh day of June, 1948, and ending on the Eleventh day of June, 1949, at the total rent or sum of Nine Hundred Dollars, payable \$75.00 in advance on the Eleventh day of each and every calendar month.

Received Two hundred and twenty-five Dollars. First month and last two months to be paid in advance.

Paid June, 1948, and April and May, 1949.

Lessee agrees to pay the gas and electric bills as

(Testimony of Lavonne Lynch).

part of agreement for rent under ceiling.

Hot water to be furnished by lessor for the first six months of lease unless lessor moves. After this period to be paid for by ten tenants, unless otherwise agreed, at rate of \$1.00 per month.

It is further understood that no linens are furnished.

Lessee agrees to give possession of all rooms at end of lease unless otherwise agreed in writing.

And the said Lessee hereby covenants to pay the said Lessor the said rent, herein reserved in the manner herein specified. And not to make or suffer any alteration to be made therein without the written consent of the Lessor.

And it is agreed that if any rent shall be due and unpaid, or if default shall be made in any of the covenants herein contained, then it shall be lawful for the Lessor to re-enter the said premises and to remove all persons therefrom.

And That at the expiration of the said term or any sooner determination of this lease, the said Lessee will quit and surrender the premises hereby demised, in as good order and condition as reasonable use and wear thereof will permit, damages by the elements excepted. And if the Lessee shall hold over the said term with the consent expressed or implied, of the Lessor, such holding shall be construed to be a tenancy only from month to month.

The lessee acknowledges the house and furniture

(Testimony of Lavonne Lynch).

are in good condition and clean and agrees to leave it the same, and to pay for any damage to property or furnishings.

In Witness Whereof, the said parties have hereunto set their hands and seals the day and year first above written.

/s/ MRS. DOROTHY SHARP,

/s/ A. J. LYNCH,

/s/ MRS. A. J. LYNCH.

Received September 9, 1948.

Admitted February 24, 1950.

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Q. (By Mr. Scheir): Now, Mrs. Lynch, at the time you rented accommodations at 430 Daisy Avenue, Long Beach, what did your family consist of?

A. My daughter, my husband and myself.

Q. How old is your daughter?

A. She is now sixteen.

Q. Did you rent these accommodations furnished or unfurnished? [18]

A. Furnished.

Mr. Matot: I move to strike it. The lease speaks for itself.

The Court: Sustained.

Q. (By Mr. Scheir): Mrs. Lynch, will you please describe the furnishings in each room in this accommodation?

(Testimony of Lavonne Lynch).

Mr. Matot: I object to that question on the ground it is incompetent, irrelevant and immaterial and has no bearing on the issues before this honorable Court.

The Court: Sustained.

Mr. Scheir: If the Court please, may I be heard on that? It appears the defendant is contending this place was rented as rooms.

The Court: Aren't you anticipating the defense? Suppose you wait until the defense goes in.

Mr. Scheir: I was trying to speed it up. Very well.

Q. (By Mr. Scheir): Mrs. Lynch, when you rented the accommodations at 430 Daisy Avenue from Mrs. Sharp, what was the arrangement as to payment of the rent?

Mr. Matot: We object to that on the ground the lease speaks for itself.

The Court: Sustained.

Mr. Matot: It is all in the lease.

The Court: Sustained.

Mr. Scheir: May I see the lease again, please?

The Court: Of course, if there is a contention she didn't pay the rent——

Mr. Scheir: No, there isn't, your Honor.

The Court: That isn't the argument, is it? She



(Testimony of Lavonne Lynch).

signed the lease, the lease is the contract, and you either stand or fall on the lease. I assume all the payments were made, at least, you are bringing an action to recover on the theory the payments were made.

Mr. Scheir: If counsel will stipulate that in addition to the rent there was a cleaning charge of \$25.00, I will not pursue the matter further.

Mr. Matot: I will stipulate to nothing whatever.

Mr. Scheir: Very well.

Q. Mrs. Lynch, how did you pay the rent?

Mr. Matot: Now, I object to that on the ground it is incompetent, irrelevant and immaterial. The lease is the best evidence, your Honor.

The Court: Overruled.

The Witness: We paid the first month and the last two months of the lease in one check, plus a twenty-five dollar cleaning deposit.

Q. (By Mr. Scheir): And how did you pay the rent for the succeeding months?

A. \$75.00——

Mr. Matot: I object to that as incompetent, [20] irrelevant and immaterial.

The Court: Overruled.

Mr. Scheir: If your Honor please, I am trying to establish my case.

The Court: Overruled.

Mr. Scheir: Will you answer?

The Witness: We paid each month on the 11th of the month.

Q. (By Mr. Scheir): By a check or cash?

(Testimony of Lavonne Lynch).

A. By check.

Q. How much did you pay each month after the first month?

A. We paid \$75.00 for the—I have to count on my fingers—for the first six months, and the following five we paid \$76.00, because she asked a dollar extra for the gas and water heater the last six months.

Q. Now, Mrs. Lynch, I show you a series of checks, ten in number, and ask you if these are the checks which you gave to **Mrs. Sharp in payment** of the rent and the cleaning fee?

Mr. Matot: Wait a minute. I object to the question. It assumes something not in evidence. It says "rent and cleaning." I object to the question.

Mr. Scheir: Your Honor, the witness testified she paid a cleaning fee of \$25.00.

The Court: Overruled.

The Witness: They are. [21]

Mr. Scheir: If the Court please, I offer these ten checks in evidence as Plaintiff's exhibit next in order.

The Court: They may be received.

The Clerk: No. 7.

(The documents referred to were marked "U. S. Exhibit No. 7," and were received in evidence.)

Mr. Scheir: I have no further questions of this witness, your Honor.

(Testimony of Lavonne Lynch).

Cross-Examination

By Mr. Matot:

Q. Now, Mrs. Lynch, did you ever live in this apartment prior to the 11th day of June of 1948?

A. I did not.

Q. Now, at the time you and your husband signed this lease, did you read it carefully before you signed it?

A. We did.

Q. You know everything that was contained within that lease?

A. I believe so.

Q. Now, during the first month, from the 11th day of June, 1948, to the 11th day of July, 1948, how many persons did you have living with you in that accommodation?

A. There were three persons living in that accommodation.

Q. Isn't it a fact that you had some six persons living there with you for one month, other than the three persons in [22] your immediate family?

A. That is not true.

Q. They were never there at any time?

A. They did not live there.

Q. Well, what do you mean they didn't live there?

A. We had guests for a couple of nights, but they did not live there.

Q. How many nights?

A. We had a family of guests for two nights, one night with the permission of the landlady, and——

Q. I am discussing now about June 11th to July 11th.

(Testimony of Lavonne Lynch).

A. We did not have any guests during that time——

Q. No guests?           A. ——that I recall.

Q. Very well. When was the last month you paid rent under this lease?

A. From May 11th to June 11th, 1949.

Mr. Matot: O. K., that is all.

Mr. Scheir: No further questions, Your Honor.

(Witness excused.)

The Court: Call your next witness.

Mr. Scheir: Mrs. Gutierrez. [23]

### LILLY GUTIERREZ

called as a witness by and on behalf of the Plaintiff, having been first duly sworn, was examined and testified as follows:

The Clerk: Your name, please.

The Witness: Lilly Gutierrez.

The Clerk: Please be seated.

### Direct Examination

By Mr. Scheir:

Q. Mrs. Gutierrez, you were formerly Lilly Dolci, is that correct?           A. Yes.

Q. Have you ever lived at 537 Melrose Way in Long Beach, California?           A. Yes, sir.

Q. During what period of time did you live there?

A. I paid rent from November 5, 1947,——

Mr. Matot: I move to strike it on the ground it is not responsive.



(Testimony of Lilly Gutierrez.)

The Court: Denied.

The Witness: —and I lived there until October of nineteen-forty—well, I was married and I moved out I think in '48.

Q. (By Mr. Scheir): During the time you lived there, to whom did you pay your rent?

A. Mrs. Dorothy Sharp. [24]

Q. And how much did you pay?

A. I paid \$30.00 for the first two months, and twenty-nine thereafter.

Q. In addition to the thirty-dollar payment, were there any additional charges?

A. \$5.00, cleaning charge.

Q. Were these premises rented to you furnished or unfurnished? A. Furnished.

Q. Now, Mrs. Gutierrez, I show you two receipts, one dated November 5, 1947, the other December 5, 1947, and ask you from whom you obtained those receipts?

A. I obtained the first one from Mrs. Sharp—both of them from Mrs. Sharp; but the one that has "Cleaning charges paid," she had given me that receipt later, but I had actually paid her mother and she gave me written receipt for the rent and that charge after that.

Q. Do these two receipts represent the rent for the month of November and the rent for the month of December and the cleaning charge?

A. Yes, sir.

Mr. Scheir: If the Court please, I offer these two receipts as Plaintiff's exhibits next in order.



(Testimony of Lilly Gutierrez.)

The Clerk: No. 8.

The Court: They may be received. [25]

(The documents referred to were marked "U. S. Exhibit No. 8," and were received in evidence.)

Mr. Scheir: I have no further questions, your Honor.

The Witness: May I say something?

The Court: No; I am sorry.

The Witness: I have plenty to say.

### Cross-Examination

By Mr. Matot:

Q. Now, when you moved in there, Mrs. Gutierrez, you saw another bed that you wanted, didn't you, in that house? A. No, I did not.

Q. And isn't it a fact that Mrs. Sharp charged you a dollar for giving you a different bed?

A. That is not true. I didn't see the bed until I actually moved into the house and paid the rent.

Q. You didn't ask her to move a bed in extra for you? A. No.

Q. And you did not pay \$1.00 extra for this bed?

A. She had what you might call a Hollywood studio couch, and said it was a new couch, and asked me if I would be willing to pay a dollar extra for that until it was paid for. I said I would do that, because I wanted a place to stay.

Q. So you actually paid this dollar to get that other bed? A. Yes. [26]

Mr. Matot: That is what I wanted.

(Testimony of Lilly Gutierrez.)

Redirect Examination

By Mr. Scheir:

Q. Mrs. Gutierrez, did you rent these accommodations furnished or unfurnished?

A. Furnished.

Q. Was there another bed in there at the time, other than this Hollywood bed?

A. There was not.

Mr. Scheir: I have no further questions.

Mr. Matot: Nothing further, your Honor.

The Court: You may step down.

The Witness: I can't say anything?

The Court: No.

(Witness excused.)

The Court: How many witnesses do you have, Mr. Scheir?

Mr. Scheir: That is my case.

The Court: How many witnesses do you have, Mr. Matot?

Mr. Matot: About three.

The Court: It is twelve o'clock. We will recess until two o'clock this afternoon.

(Whereupon, at 12:00 o'clock noon, a recess was taken until 2:00 o'clock p.m., of the same day.) [27]

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Friday, February 25, 1950

Mr. Matot: If your Honor please, the plaintiff having rested, it is now our intention to argue a motion for non-suit.

The Court: Mr. Matot, I am not interested in any argument you may make at this time. I want all the evidence before the Court. You are wasting the Court's time by making an argument at this time.

Mr. Matot: Very well. I merely want to protect the record.

The Court: The record may show you offered to make an argument and I have discouraged it.

Mr. Matot: Very well.

Mrs. Sharp, will you take the witness stand.

### DOROTHY SHARP

a defendant herein, called as a witness in her own behalf, having been first duly sworn, was examined and testified as follows:

The Clerk: Your name is——

The Witness: Dorothy Sharp.

The Clerk: Take the stand.

### Direct Examination

By Mr. Matot:

Q. Mrs. Sharp, will you state your full name?

A. Mrs. Dorothy Sharp. [28]

Q. Where do you reside?

A. 428 Daisy Avenue, Long Beach.

Q. And are you the defendant in this action?

A. Yes.

Q. And you are the owner of the property described in this complaint? A. Yes.

Mr. Matot: May I have Exhibit No. 5, I believe, the newspaper.

Q. Now, Mrs. Sharp, I will show you at this time Plaintiff's Exhibit No. 5, which is a copy of the

(Testimony of Dorothy Sharp.)

classified ad section of the Long Beach Independent, and call your attention particularly to the ad marked here in red.           A. Yes.

Q. Now, did you put that ad in the paper, Mrs. Sharp?

A. Yes. May I look at it just a moment to see if I see something else on here?

Q. Yes.

A. Pardon me a moment; I have to run down these quickly. There is also another ad in here I placed the same day, running in the paper the same day.

I find one here——

Q. Will you read the other ad you put in on the same day?

A. Yes. I advertised rooms. In this case I took one specific room and advertised it. Then, of course, I talked [29] to the people, naturally, regarding it, and if they didn't want it I had two others, or one other, and instead of advertising them both I just put one ad in.

Q. What did the other ad refer to?

A. The rooms I had for rent.

Q. No, the first one.

A. My own duplex. I lived in my own duplex.

Q. You covered that one by the other ad, did you?

A. No. Maybe I am not understanding you correctly.

Q. Which duplex did the first one refer to, your own, or the one under consideration here in this suit?



(Testimony of Dorothy Sharp.)

A. The first one mentioned here, identified in red, is my own duplex; and——

Q. Where you were living, you were going to rent that?

A. I had considered it. Briefly, I would need to explain that, probably, to the Court. That ran the one day only. I had been advertising for several days—If I had the papers here, I could show The Independent people—if they brought their correct records of my whole advertising, they would show that (indicating) had been running, “Exceptionally private studio room for lady; clean quiet. Laundry, kitchen. Close in. Phone 64-1123.”

Q. That was the one involving your room?

A. Yes.

Q. And this (indicating) was the one in which you were [30] contemplating renting your own apartment?

A. Yes.

Mr. Scheir: Your Honor, I object to this whole line of testimony as being leading. I don't mind the witness answering the question, but I do object to the leading and suggestive questions.

The Court: Overruled.

Q. (By Mr. Matot): Now, Mrs. Sharp, when and where did you meet the tenants known as A. J. Lynch and Mrs. A. J. Lynch?

A. I believe the first time I seen them I was already in the duplex where the rooms are, and my—ordinarily, you will notice, in both ads I gave only my phone number, and I talk to people on the phone.

This was a very great exception, when my daugh-



(Testimony of Dorothy Sharp.)

ter answers the phone; and even though she knows I usually do that, I was in the other side of the house and I had been called back so often, and the people seemed to be very anxious, she said, so she gave the address, and they came right over.

I was there showing it to somebody else, and it seems before I left they came to the door, as I was leaving. I don't believe I talked to them at my house at all. I thought they wanted to see the rooms, and I remember very distinctly we were standing in the kitchen of the duplex in question, where the rooms are, when I realized they wanted to know about the duplex. They seemed to like the place, and I went ahead [31] and showed it to them.

And I would like a chance to explain to the Court, before this becomes confusing, about the ad on the duplex.

Q. Go ahead.

A. I put it in the night before. You can only cancel your ad up to twelve o'clock, but you can put them in up to four-thirty. I had, on the spur of the moment, decided I would move back where the rooms were, to that side, and rent the side I was in, which I had done four years previously. I put the ad in, but couldn't take the other out.

Meantime, I knew I had to hurry and make a quick decision and get it in before four o'clock for the deadline. So I done that, and couldn't take the other out. Then I decided, in the meantime, I would stay as I was, and when these people were already in the house, and they seemed to like it, I talked with

(Testimony of Dorothy Sharp.)

them about it, and they seemed to want it; and as far as the rooms go, I even had one person in there then where the rooms were.

Q. Go ahead. What was your conversation with the Lynches as to these rooms?

A. Well, I told them there were three rooms, and I said, "That is the only way my OPA are," and I said, "I don't care to change it on my set-up here." I said if they wanted to take the three rooms I didn't know of any reason why they couldn't. And I insisted—I wanted to show them the OPA, [32] and they said "No."

I said I was very tired looking after the three rooms, and it would give me a little rest, if they want to take them and assume all utilities and about one hour a week vacuuming through the center of the house, I would reduce——

Q. What was the OPA ceiling on those rooms at that time?

Mr. Scheir: I object to that. The official records are in evidence and speak for themselves.

Mr. Matot: Very well. May I have Defendant's Exhibit A.

Q. Will you look at this schedule and tell me what your OPA rental was on those rooms on June 1st of 1948?

A. Well, I am afraid I did not—This is the schedule for my rooms.

Q. What would that amount to by the month? ,

Mr. Scheir: I object to that, your Honor.

(Testimony of Dorothy Sharp.)

The Witness: The total was about ninety-five or ninety-eight dollars——

The Court: Just a moment.

The Witness: I am sorry.

Mr. Scheir: I object to that, your Honor. The records are in evidence and they speak for themselves.

Mr. Matot: She is testifying from the record, your Honor. [33]

The Court: Overruled.

Q. (By Mr. Matot): \$95.00 a month?

A. Well, it was over that.

Q. Well, it was at least \$95.00 a month under that schedule before you?

A. As I figured, the very least it could be—It made a difference how many people were in and according to whether they had kitchen privileges or not, so I never figured what the very least was, but it was around that.

Q. So you told them they could have it for \$75.00, which you figured was about \$20.00 under the OPA ceiling?

Mr. Scheir: I object to that, your Honor. It calls for a conclusion of the witness.

The Court: Overruled.

The Witness: My operating expenses were about eight——

Q. (By Mr. Matot): No, answer the question. Read the question, please.

(The question was read.)

A. Yes.

(Testimony of Dorothy Sharp.)

Q. And this is the lease you entered into with them for those rooms, Plaintiff's Exhibit 6?

A. Yes, this is the lease.

Q. Now, Mrs. Sharp, when did you get a letter or a command subpoena from the Office of the Housing Expediter after the execution of this lease? [34]

A. It was in January, 1949.

Q. And what matter did they call you in on?

A. On a matter of another rental. It was a matter of \$6.00 they claimed were overcharged.

Q. No mention was made about this Lynch arrangement at that time?

A. No. I never did receive any letters——

Q. When did you first hear about this Lynch situation?

A. After I was in the office and talked to him about this \$6.00, which he very quickly admitted was of very little merit, but then immediately took up the matter of the Lynches.

Q. I will show you here a document, the original of which is Plaintiff's Exhibit No. 3. Now, will you tell me whose handwriting this is in?

A. Well, this is the OPA that was made out, but I believe his name is Mr. Wilson in the OPA office, on January 14th. I dated it myself at the bottom, when I signed it.

Q. How did you come to sign that document, Mrs. Sharp? Tell us what happened.

Mr. Scheir: If your Honor please, I will object to this line of testimony inasmuch as it has been well established in an action of this kind the validity of



(Testimony of Dorothy Sharp.)

the order issued by the area rent office cannot be attacked unless the tenant has exhausted his administrative remedies. Unless that has been done, any effort to attack the validity of the order [35] is admissible.

The Court: Overruled.

Q. (By Mr. Matot): Go ahead and tell us.

A. Well, Mr. Wilson brought this up, and he said the people being related was the reason I couldn't rent to them. Well, I said I had never heard of any such ruling, and after all I dealt with the OPA for a good many years, so I asked to see it; and he hunted down and in the bottom drawer of the bottom of the desk he found a book, and in the middle of the paragraph, in very fine print, he read something that might have been interpreted that I couldn't. But I have never seen it published, and had no idea there was any such——

Q. Tell me what he said he was going to do to you if you didn't sign it.

A. Well, he was going to sue me, and what not. However, he led me to believe—He said that if I would sign it that he would—well, they would take it as though it were a new registration of an apartment and handle it as though it were. He led me to believe that, and they would establish, after a fair investigation, establish a ceiling.

Q. What else did he tell you about it? If you didn't sign it, what would he do? I want you to tell us about that.

A. Well, yes, he—Well, I was rather provoked



(Testimony of Dorothy Sharp.)

that I hadn't been sent any letter, and I asked why, and he couldn't explain why they hadn't sent me a letter all this time. [36] Always before I had received one from them very promptly. And I told him, "I have never rented it any other way. I don't see why I should have to change my OPA. Why are you making me do this when I have never rented it at any time during my ownership other than rooms?"

And he just said they would sue me if I didn't, and I had to.

Q. Later on you went back to file an appeal, didn't you?      A. Yes.

Q. And what did this man tell you then?

A. Well, I made an appointment myself to talk to the head of the OPA, and I went in of my own accord to file an—I wanted to talk it over with him before I appealed their action in the matter, which was more than merely unfair. It was a matter of a great deal of spite and prejudice mixed in.

Mr. Scheir: Your Honor, I move that portion of the answer be stricken.

The Court: It may go out, the last part.

Q. (By Mr. Matot): What did he say you had to do before you could file the appeal?

A. I had to deposit the full amount of money with him or I couldn't file an appeal. That is printed on the back of the notice I received.

Q. Did anybody other than you hear him make that statement? [37]

A. There was no one with me. There was only his secretary in and out of the room. But that is

(Testimony of Dorothy Sharp.)

printed on the back of the form they sent me, that I had to deposit the money in order to make the appeal.

Q. I show you this document, and will you show me where it says anything about requiring you to——

A. It is not on that paper; it is another paper. You might not have that paper. It is one they sent me.

Mr. Scheir: I believe it is on the order itself, your Honor, which is Plaintiff's Exhibit No. 3. It is a photostatic copy of an order.

The Witness: I have 3.

Mr. Scheir: No, it is No. 4.

The Court: There is nothing on the back of 4.

Mr. Scheir: That (indicating) is the original.

Mr. Matot: Your Honor, I call your attention to the fact that this exhibit No. 4 is not a complete copy of the original.

Mr. Scheir: Your Honor, evidently the back was not photostated, in which event I will submit the original and ask leave to withdraw it at the conclusion of the trial.

The Court: That will be the order.

Q. (By Mr. Matot): Will you show me on the back of this order where it provides that you must deposit the amount of [38] the overcharge before you can appeal?

A. Just one moment. Well, it does list—I don't know if I am reading too hastily or if this is the one:

“Failure on your part to make the refunds within

(Testimony of Dorothy Sharp.)

the 30-day period above mentioned is a violation of the Rent Regulations and this Order and may subject you to suit for three times the amount.”

Q. Well, did he tell you——

A. He told me that, and I was sure I had read it on the back of one of the papers. He did tell me that, because that was one of the first things he said when we started to talking, that I had gone three days over the time to possibly refund, and we discussed the matter.

I said I didn't have the money to deposit, either. He didn't have anything to say to that, that I couldn't even appeal it because I didn't have the money to deposit.

Q. Did you sign this of your own free will, or did this man Wilson force you to sign it?

Mr. Scheir: I object to that. That calls for a conclusion on the part of the witness. The Court has heard the testimony concerning this conversation, and should make his own decision.

The Court: The question, as I understand, is “Did you sign this?” What do you mean this “this?”

Mr. Matot: I mean Plaintiff's Exhibit 3, which is the [39] registration certificate which she is alleged to have signed.

The Court: Is that your signature?

The Witness: Yes.

Mr. Matot: Will you read my question?

(The question was read.)

(Testimony of Dorothy Sharp.)

The Witness: I am willing to let it stand on whatever the Court thinks.

Q. (By Mr. Matot): What did you do? Did you sign that of your own free will or not?

A. No, I don't think you could say that possibly.

Q. You didn't want to sign it? A. No.

Mr. Scheir: If your Honor please, I object to counsel leading the witness. I also object to asking a question which calls for the conclusion of the witness.

Now, whether or not she was forced to sign it is a matter for determination by the Court. Being threatened with suit, in my opinion, is not coercion.

The Court: Overruled.

Q. (By Mr. Matot): Would you have drawn one of those up and signed it, of your own free will, and sent it in?

A. No. I am very sure if I had left the office I never would have made it out.

Q. This is in the handwriting of the officer of the OPA? A. Yes. [40]

Mr. Matot: You may take the witness.

### Cross-Examination

By Mr. Scheir:

Q. Mrs. Sharp, did you read this registration statement before you signed it?

A. He asked me the questions, wrote it out himself, and pushed it to me.

Q. The information appearing on the registration statement is true?

A. Yes, I believe it is.

The Court: May I see that?



(Testimony of Dorothy Sharp.)

Mr. Scheir: May I have the lease, your Honor?

Q. Mrs. Sharp, how many rooms does this part of the duplex contain, that is, the part you rented to the Lynches?

A. Two bedrooms. It contains three rooms for renting, or, if used for a home, is generally considered as two bedrooms.

Q. How many rooms does the unit itself contain?

A. Five rooms.

Q. What are those rooms?

A. Living room, two bedrooms, or, in this case, it was used as a studio room and two bedrooms.

Q. What else?

A. Kitchen and bath, and an extra sitting room upstairs; we call it a den. [41]

Q. Are all the rooms located on one floor?

A. No.

Q. Two floors?           A. Yes, sir.

Q. What is located on the first floor?

A. A studio, a kitchen, and bath.

Q. What rooms are on the upper floor?

A. Two bedrooms and a sitting room.

Q. These rooms were rented to the Lynches furnished, is that correct?           A. Yes.

Q. What furniture did you have in the kitchen when the Lynches rented the place?

Mr. Matot: I object to that, incompetent, irrelevant and immaterial, and outside the issues raised here.

The Court: Overruled.



(Testimony of Dorothy Sharp.)

The Witness: The same as had always been there and is still there.

Q. (By Mr. Scheir): I wish you would explain what you mean by that. What furniture was there?

A. You want me to name each piece?

Q. Yes, if you can.

A. Stove, and refrigerator, table, and three chairs. The rest is built in.

Q. What furniture did you have in what you call the [42] sitting room?

A. A divan, chair, large library table, rugs, a desk and a small oval table.

Q. What furniture did you have in the rooms upstairs?

A. The bedrooms now? I was describing the sitting room upstairs.

Q. I mean the room downstairs. You have described the furniture in the kitchen. You say you have another room downstairs. What furniture is in that room?

The Witness: Would you mind if I say something?

The Court: Answer the question.

The Witness: All right, I will do it the hard way. Downstairs, in the studio room—which might have been called the living room, according to how they want to use it—was a studio divan, and there was a table—Oh, dear. I traded with them one piece of furniture.

The Court: Is there any contention, counsel, that these apartments weren't furnished?

(Testimony of Dorothy Sharp.)

Mr. Scheir: No. I am merely bringing out——

The Witness: I changed a piece of furniture.

Mr. Scheir: ——the way the apartments were furnished, to show it was rented as an entire unit.

Mr. Matot: I don't see how you can show that by this testimony.

The Court: I don't see how this is material. [43]

The Witness: It had a dresser in it when they took it, in the studio room, and for their convenience I took it out and gave them a table they could make a dining room, since they had no dining room.

Q. (By Mr. Scheir): Mrs. Sharp, will you point out to me the ad which you read to the Court before when counsel was questioning you?

A. Yes (indicating). "Exceptionally private studio room for lady; clean, quiet. Laundry. Kitchen. Close in. Phone 64-1123."

Q. Which room did that ad pertain to?

A. The studio room. It was a living room, or, if used as a family dwelling, it would be used as a living room, naturally.

Q. To which apartment did the other ad pertain?

A. To my own home.

Q. You never moved from that apartment, did you?      A. No.

Mr. Matot: I object to that, incompetent, irrelevant and immaterial.

The Court: Overruled.

Mr. Scheir: You may answer the question.

The Witness: I answered it "No."

Q. (By Mr. Scheir): Now, I call your attention

(Testimony of Dorothy Sharp.)

to the lease which you entered into with Mr. and Mrs. Lynch, which [44] lease bears your signature. I call your attention to that part of the lease which reads, "Lower room—Upper front—Upper middle—Upper rear." Which one was the upper room?

Mr. Matot: I object, incompetent, irrelevant and immaterial because the lease speaks for itself.

The Court: Overruled.

Q. (By Mr. Scheir): Which was the lower room? A. The studio room. Those——

Q. Just a minute. Which one was the upper front?

A. That was the upper front bedroom.

Q. Which was the upper middle?

A. The room referred to as the sitting room. It at one time had an OPA on it.

Q. Which was the upper rear?

A. Upstairs rear bedroom.

Q. The lease further reads, "Including kitchen and bath." Were there any rooms in addition to these rooms in the apartment?

Mr. Matot: I object to that, incompetent, irrelevant and immaterial.

The Court: Overruled.

The Witness: No.

Q. (By Mr. Scheir): So that at the time you advertised the studio room for rent, you had no other room other than the rooms which appear on this lease and which you rented to the [45] Lynches, is that correct?

(Testimony of Dorothy Sharp.)

A. In that, no other rooms for rent except in that unit.

Q. By this lease you rented the entire unit to the Lynches, is that correct?

A. That would have given them possession if they rented all three rooms.

Q. In other words, the Lynches had the entire unit; there was no other space left that they did not occupy in that unit, is that correct?

Mr. Matot: I object, your Honor, incompetent, irrelevant and immaterial, and calling for the conclusion of the witness.

The Court: Overruled.

The Witness: That is correct.

Q. (By Mr. Scheir): Now, Mrs. Sharp, who paid for the utilities while the Lynches were living at 430 Daisy Avenue?

A. Well, I paid for—They paid their own electric bill and gas bill for their cooking and heating. I furnished the hot water, except they paid one month. They paid \$1.00 for one month.

Q. There was a separate meter for this apartment, was there not, for the gas and electricity?

A. Yes, and I furnished the water.

Q. Is that correct, there was a separate meter?

A. Yes. [46]

Q. And the Lynches paid for the gas and electricity which was shown on that meter, is that correct? A. Yes.

Mr. Scheir: I have no further questions.

Mr. Matot: No questions.



(Testimony of Dorothy Sharp.)

The Court: May I ask the witness a question?

Mr. Matot: Certainly.

The Court: You had a duplex, and you occupied one side and rented the other?

The Witness: Yes.

The Court: Which side did you occupy?

The Witness: 428 Daisy is my residence.

The Court: What is 537?

The Witness: That is on Melrose Way, on a side street, a small apartment that faces the side street, Melrose Way.

The Court: Is that a different building?

The Witness: Yes, a different building.

The Court: And this at 430 was a duplex?

The Witness: Yes.

The Court: And you occupied one side and you rented the other?

The Witness: Yes, as rooms. Under OPA, as rooms only. I have never had——

The Court: Was it under OPA as an apartment in——

The Witness: Before the Lynches moved [47] in?

The Court: Yes.

The Witness: No, it wasn't. I had lived there four years myself.

The Court: Did you ever rent it as an apartment?

The Witness: No, never. I moved out in 1946 to 428 Daisy. I fixed it up to rent as rooms, and I never rented it in any other way.



(Testimony of Dorothy Sharp.)

The Court: Do you rent the other side as an apartment?

The Witness: The side I was living in, 428 Daisy, had been a single family dwelling.

The Court: How much did you get for that?

The Witness: That OPA in '42 was fifty-five.

The Court: \$55.00?

The Witness: Yes. The two are quite different. That is all on the lower floor, and the other is upper and down, and there is quite a bit more square footage on that side.

The Court: Did you own the apartment when it was originally registered with OPA?

The Witness: Yes, I did.

The Court: And was 430 Daisy listed as rooms at that time?

The Witness: No, that was—there was no listing, because it wasn't under OPA when I bought it.

The Court: You were living in it?

The Witness: Yes. [48]

The Court: When you moved out of it, did you list it as rooms or did you list it as an apartment?

The Witness: As rooms. I have in a valise—I guess I left it in the car—the original registration on rooms, the very first one, prior to the one we have in court today. That brought considerably more than that originally, and that has on it the date of the original registration of rooms—I believe it was August, 1946—when I moved out. I had lived there four years, and moved out of it, and

(Testimony of Dorothy Sharp.)

registered it as rooms at that time. That was the original registration.

The Court: Maybe, if it was registered as rooms originally, the plaintiff has a copy of the registration.

Mr. Scheir: We have, your Honor; but inasmuch as the maximum rents shown on this registration statement have been changed by order, we did not offer it in evidence. However, I have it here, if the Court wishes to see it.

The Court: I think the question here is whether this was registered as rooms or an apartment.

Mr. Scheir: No, the question is, how were these housing accommodations rented to the Lynches?

Mr. Matot: No, your Honor, that wouldn't be the point at all.

Mr. Scheir: Housing accommodations may be rented——

The Court: I don't agree with you. I think your lease is subject to the rent control, and it depends a great deal as to what the ceiling price was. [49]

Now, we have one registration showing it was registered as an apartment at \$75.00 a month, but that evidently was in 1949—or a 1948 registration, June 11, 1948. Now, what was the status before June 11, 1948?

Mr. Scheir: Before June 11, 1948, individual rooms had been rented out to individual people. The house accommodations had been rented as rooms under the rooming house regulation.

(Testimony of Dorothy Sharp.)

Here we have a different situation. We contend the place was rented as a unit, therefore it had to be registered under the housing regulations.

We have two regulations; one is for rooms in a rooming house, and one is for apartments. Therefore we obtained a registration statement from the defendant here registering the apartment as an apartment.

The Witness: After they had possession——

The Court: Can you agree that before June 11, 1948, the housing accommodations were rented out as rooms?

Mr. Scheir: We have no way of knowing otherwise. We agree that up until the time the Lynches rented the apartment the place had been rented as individual rooms. It had been registered under the rooming-house regulations.

Now, when the house is rented as an entire unit, it must be registered under the housing regulation.

The Court: Let me see that. [50]

Mr. Matot: Let me call your Honor's attention——

The Court: Just a minute.

Mr. Matot: Certainly.

The Court: Was this registration, which is Exhibit 3, was that obtained after the premises were leased to Mr. and Mrs. Lynch?

Mr. Matot: Seven months after.

The Court: Just a minute, Mr. Matot. I am talking to counsel.

Mr. Matot: Pardon me.

(Testimony of Dorothy Sharp.)

Mr. Scheir: Yes, your Honor, it was.

The Court: Now, can you tell me when it was obtained? I have a date here, "Date first rented June 11, 1948," but when was this obtained, do you know?

Mr. Scheir: This was obtained, your Honor, January 14, 1949. The defendant has testified she put the date on here after she signed or at the same time she signed the registration statement.

Now, in that connection,——

The Court: In other words, then, until January 14, 1949, these were rooms?

Mr. Scheir: They had been rented as rooms, yes, your Honor.

The Court: And this was retroactive back to June 11th?

Mr. Scheir: To the date of first renting as an apartment. [51] We did not go beyond June 11th, because the Lynches were the first ones who rented it as an apartment, on June 11th.

The Court: Now, Exhibit 4, which is the order decreasing rent, that was issued March 23d?

Mr. Scheir: That is correct, and was made retroactive to the date of the first renting as an apartment, which was June 11, 1948, I believe.

In that connection, your Honor,——

The Court: I am not interested in argument now. I am interested in trying to find out what the facts are. I am trying to find out what the facts are, then I can come to some conclusion; but I can't unless I know what the facts are.



(Testimony of Dorothy Sharp.)

Mr. Scheir: I have no further questions of this witness, your Honor.

Mr. Matot: I have no further questions.

The Court: You may step down.

(Witness excused.)

Mr. Matot: My other witness stepped out. May I step out of the court room and see if I can find him?

The Court: Yes, you may.

Mr. Matot: One of my witnesses went to the car across the street to get those papers. I wonder if we can recess for five minutes.

The Court: We will take a recess but, before we do that, [52] have you got the original registration on rooms? I notice on Exhibit 3 it says, "This unit formerly rented as rooms."

Mr. Scheir: Yes, I have, your Honor.

The Court: I wonder if you would mind introducing it in evidence.

Mr. Scheir: Your Honor, may I again ask leave to withdraw the original at the conclusion of the trial?

The Court: Yes.

The Clerk: No. 9.

(The document referred to was marked "U. S. Exhibit No. 9," and was received in evidence.)

The Court: May I clarify something, too. My understanding from your statement is that these rooms had been rented prior, but had been rented to different individuals?



Mr. Scheir: That is correct.

The Court: Then, instead of renting rooms to different individuals, they rented all the rooms to the Lynches?

Mr. Scheir: To the Lynches; that is correct.

The Court: Then I assume it is your contention that because all the rooms were leased to one party instead of to three different parties, or four, it immediately changed the complexion of the renting from rooms to an apartment?

Mr. Scheir: That is correct, your Honor. Under the rooming-house regulation only rooms could be rented. So as the complexion of the thing was changed to an apartment, [53] if it could not come under the housing regulation it would be uncontrolled.

Mr. Matot: Let me say, your Honor, supposing you were living at the Biltmore under the rooming regulation, and your wife moved next door, do you mean that would change those two rooms to an apartment? I say, "No."

The Court: Is your witness in court now?

Mr. Matot: Yes.

### ALBERT ABRAMS

called as a witness by and on behalf of the defendant, having been first duly sworn, was examined and testified as follows:

The Clerk: Your name, please?

The Witness: Albert Abrams.

Mr. Matot: You should apologize to Judge Westover for wandering out of the court room.

(Testimony of Albert Abrams.)

The Court: He doesn't have to apologize.

Go ahead; let's get this over with.

Direct Examination

By Mr. Matot:

Q. Mr. Abrams, do you know Dorothy Sharp?

A. I do.

Q. How long have you known her?

A. I would say about five years.

Q. Did you go to the Office of the Housing Expediter in the City of Long Beach on or about the 14th day of January, [54] 1949?

A. Yes.

Q. Were you present there when Mrs. Sharp signed a registration?

A. I was there when she was supposed to sign it. Now, she signed it on the other side of a partition from me.

Q. But did you hear the conversation——

A. I did.

Q. ——between Mrs. Sharp and this other man?

A. I did.

Q. Will you tell us what the conversation was?

Mr. Scheir: I object to that, your Honor, again on the ground the validity of the order cannot be attacked in this action unless the administrative remedies have been resorted to first.

The Court: Overruled.

The Witness: Well, I tell you, I will try and be just as brief on this as I can, your Honor. I went in there with Mrs. Sharp about two o'clock, and had an appointment at four, and I listened for pos-

(Testimony of Albert Abrams.)

sibly an hour or an hour and a half, and I became very uneasy because of this appointment, and sent a note in.

Up to that time I can't truthfully say I had overheard any of the conversation except just in a mumble, or a tone I couldn't understand, at least. [55]

When I sent this note in, Mrs. Sharp told me afterwards it disturbed her very greatly.

Mr. Scheir: I object to that as hearsay.

The Court: Hearsay. Objection sustained.

Q. (By Mr. Matot): Just tell us what you heard Mrs. Sharp say and what this gentleman said.

A. This gentleman at that time assured Mrs. Sharp if she wouldn't sign the papers——

Mr. Scheir: I object to that. The gentleman has not been identified,——

The Witness: I could identify the gentleman.

Mr. Scheir: ——and, as far as the witness is concerned, hearsay.

The Court: Overruled. Just give us the conversation.

The Witness: He was very persuasive in telling her if she wouldn't sign the papers they would come down there and go in and put a ceiling on it anyway.

At that time I believe they had started to the door, and in the meantime Mrs. Sharp had signed the papers, apparently, because they came out and stood at the railing where we stood, and he said, "Mrs. Sharp, it is good you signed it. I think we would have forced you to sign it anyway."

(Testimony of Albert Abrams.)

Q. Mr. Abrams, what is your business or occupation?

A. I am a broker, real estate broker.

Q. How long have you been a broker? [56]

A. About twenty-five years.

Q. How long in Long Beach?

A. Since 1925.

Q. Do you live in the neighborhood where this property is located? A. I do.

Q. Are you acquainted with the neighborhood?

A. Very much so.

Q. Do you know the value of real estate?

A. Yes.

Mr. Scheir: I will object, your Honor, to this line of questioning, inasmuch as the opinion of the witness as far as the rental value of the property is immaterial in this action.

The Court: I will overrule your objection to this particular question. The question is, does he know values, and his answer is "Yes." I am not cutting you off from making your objection.

Mr. Scheir: Thank you.

Q. (By Mr. Matot): Could any property of the nature of this, in that neighborhood, have been rented at this time for \$37.00 a month?

Mr. Scheir: I will object to that, your Honor. We are not attempting to set the maximum rent here.

The Court: Sustained.

Mr. Matot: Your Honor, I want to show this, and this is [57] my reason: I understand ordinarily



(Testimony of Albert Abrams.)

an order of the OPA can not be collaterally attacked. I know that. But in this case, where we lay a foundation to impeach an order, then I think we should be able to show that she was treated maliciously.

The Court: Well, Mr. Matot, I can't agree with you. I don't think the question whether it was reasonable rental has any place in this case at all.

Mr. Matot: Very well.

The Court: The ruling still stands.

Mr. Matot: Very well.

I think that will be all.

Mr. Scheir: I have no questions.

The Witness: Thank you. I am sorry I went out.

(Witness excused.)

Mr. Matot: That is our case, your Honor.

The Court: I think we will take a little recess. We will recess until five minutes after three.

(Short recess taken.)

The Court: I think I know the theory of this case pretty well. Maybe I better hear from Mr. Matot first.

Mr. Scheir: Your Honor, I was going to put on a witness on rebuttal.

The Court: Oh, very well. Go ahead. I thought you had finished.

Mr. Scheir: Mrs. Lynch, will you take the [58] stand?

LAVONNE LYNCH

recalled as a witness by and on behalf of the plaintiff, in rebuttal, having been previously duly sworn, was examined and testified further as follows:

Direct Examination

By Mr. Scheir:

Q. Mrs. Lynch, you heard Mrs. Sharp testify that the ad you read in the newspaper pertained to 428 Daisy rather than 430?

A. That is correct.

Q. When you visited Mrs. Sharp and were shown 430 Daisy Avenue, did she show you 428 at all?

A. She did not.

Mr. Matot: Wait a minute. I think that is not proper rebuttal.

The Court: Overruled. The answer is "No."

Mr. Scheir: I have no further questions.

Mr. Matot: No questions.

The Court: All right, you may step down.

(Witness excused.)

Argument on Behalf of the Defendant

Mr. Matot: If your Honor please, I have been handling OPA work ever since 1942, and this is the first instance in which I find two different ceilings in a case. I think the [59] evidence is clear that Mrs. Sharp was called into that office for another matter. I don't think any proper proceedings were taken under the Act to change the registration from single room units to apartment units.

I think you will find in the Act, your Honor, that property can be registered one way or the other but not registered both ways. Your Honor can see more confusion would result if we permitted that kind of a situation to go on. Who would know what the ceiling price was?

As I called to your Honor's attention a while ago, suppose I had been living at the Biltmore, as a single man, and my wife moved in next door, and we got married: If Mr. Scheir's contention is good and sound, then we could force the hotel to change that from rooms to an apartment because my wife and I got married.

Now, I don't think that is good logic. I don't think the mere fact that a man and a woman are married would have any effect upon a registration already made.

Your Honor has before him the complete record to show that the property was already registered as rooms. Do you mean to tell me that because these two people were married that *ab initio* it became an apartment?

The record shows when the Lynches rented this property this lady cut the rent down \$20.00 under the then existing ceiling, so she could not be charged with any violation. [60]

The Act is not only for the protection of the tenant, but also for the protection of the landlord. If she did not charge anything over the ceiling, she should be protected. If we permit a situation of this kind, then if a party had a couple of rooms and married people moved in, why, the first thing he

knows, he would be obligated to reduce their rent, or suffer damages.

I don't think that was the intent that Congress had in mind, to destroy the landlord. The intent was to prevent a landlord from overcharging people rent. And there was no overcharge in this matter until January of 1949, about seven months after the lease ended.

How, under the regulations, could the OPA have changed that registration unless they got the landlord to sign the new registration? There is no machinery in that Act that I am conversant with that they can do that unless they could by some means get her to sign a new registration, which, I think your Honor realizes, they were out to do. They got her down on another violation—not about this case—and then they shoved these papers before her, which they make out themselves, and make her sign it. She is taken completely by surprise; and your Honor knows women are not constituted as men.

If they tried to put that over on me or over on the Court, they would know better right now. Nobody would [61] make me sign a paper or your Honor sign a paper if we did not want to. But they take a woman in there, who is trying to raise a daughter by herself, and proceed to give her a working over. I think it is a great business by some of the people down there to put the "squeeze" on this woman.

Renting a two-story apartment for \$37.00 a month in Long Beach,—it shows on the face of it. I am not charging the Housing officer with doing any-



thing wrong, but I am saying that some of the officers at Long Beach got a peeve on and were out to clean up on this woman.

I wish your Honor would keep in mind the Office of Price Administration can not change that registration without getting her to sign some document. There is no other way under the Act they can do it.

The mere fact two people are married and living in rooms wouldn't, *ab initio*, change it from one type of apartment to another kind. That can only be done by proceedings for that purpose. There is no such proceeding whatsoever here. The only thing they have got is a registration, which they prepared themselves and made her sign.

\$37.00 a month! She said she rented the other side, under OPA, for \$55.00 a month, and it is not as big as this. Your Honor, there is something wrong; there is something awful wrong. It shows intent. I say to your Honor that [62] we have two completely different registrations on this property, and that is not permissible, under the original Act or under the amendatory Act thereto. There is not one line that they have a proceeding to vacate the original order and proceed to re-register it. It couldn't be done this way. It is the same as having a case before your Honor with two judgments in it. Your Honor would never sign two judgments in the same case. I know your Honor too well from other things.

It is my opinion that the defendant should have judgment in this matter. I don't think there is any proof to support their charges.

Why hasn't a landlord a right to depend on a ceiling rate without being subjected to overcharge by another Act changing it? Where is your protection? What was the woman to do? She had three rooms ready, and she wanted to rent them. She tried to cut the rent below the ceiling, when she could have got more. I think, your Honor, we should have a judgment.

### Argument on Behalf of the Government

Mr. Scheir: Your Honor, it is not uncommon, in housing accommodations, to have more than one maximum rent, and that is why we have two regulations, the one the rooming house regulation and the other the housing regulation. [63]

The rooming house regulation, Section 825.81 (b) (iv), exempts the following housing from the provisions of its regulations:

“Entire structures or premises, as distinguished from the rooms within such entire structures or premises.”

In Section 825.81 of the rooming house regulations a room is described as follows:

“ ‘Room’ means a room or group of rooms, not constituting an apartment, rented or offered for rent as a housing accommodations unit in a rooming house, hotel or other establishment.”

In the same section, an apartment is defined as follows:

“ ‘Apartment’ means a room or rooms providing facilities commonly regarded in the

community as necessary for a self-contained dwelling unit, and of a class of accommodations customarily rented without variations in rent dependent on terms of occupancy and number of occupants: Provided, however, That a self-contained dwelling unit containing a kitchen and bath shall be deemed an apartment.”

Now, Section 825.81 exempts from the regulations all those housing accommodations except rooms in a rooming house.

Now, under the housing regulation, Section 825.1 (a) [64] (iii), the housing regulations exempts from its control “Accommodations subject to the Rent Regulation for controlled rooms in rooming houses and other establishments.” In other words, what is not controlled by one is controlled by the other. The Rooming House Regulation definitely states it applies to rooms in rooming houses, not structures or premises; and the Housing Regulation provides that it does not pertain to rooms in rooming houses but to all other housing accommodations.

Under Section 825.4 (c) of the Housing Regulation, it provides:

“For controlled housing accommodations first rented on or after July 1, 1947, the maximum rent shall be the first rent for such accommodations. Within 30 days after so renting, the landlord shall register the accommodations as provided in Section 825.7. The Expediter may order a decrease in the maximum rent as provided in Section 825.5 (c) (1) and (6).”

Now, under Section 825.7, entitled "Registration Statement," it says:

"Every landlord of controlled housing accommodations rented or offered for rent shall file in triplicate a written statement on the form provided therefor, to be known as a registration statement, \* \* \*. [65] The original shall remain on file with the Expediter and he shall cause one copy to be delivered to the tenant and one copy, stamped to indicate that it is a correct copy of the original, to be returned to the landlord."

Now, counsel for the defendant has attempted to show that the defendant was coerced into signing this registration statement. I cannot agree with him, because a person can not be coerced into doing something she is required to do by law. And I might point out that even though I don't like to file an income tax return, I do it, because if I don't I am threatened with certain punishment.

So, as regards the attack on the validity of the order of an Area Rent Director, your Honor, I would like to point out the case of *Babcock v. Koepke*, 175 Federal (2d), decided by the United States Court of Appeals for the Ninth Circuit on July 24, 1949. That was an action in which the landlord had attempted to obtain an injunction against the Area Rent Director, from issuing certain orders, and the Court held as follows, and I will quote from the opinion:

"His"—meaning the landlord—"reason for not seeking relief in the proceeding commenced



by the appellee's notice to him is that, if the appellee held adversely to him and issued his rent reduction order, appellant could have that order stayed and reviewed only [66] if he deposited by certified check or money order payable to the United States Treasurer the full amount of the refund as required by Regulation 840.11. In effect, his argument is that it is grossly inequitable requirement of a litigant to deposit before litigation the total amount of the judgment in cash, to be held by the adjudicating tribunal and if he is successful to be returned to him without interest while so wrongfully deprived of its use.

"He claims that he did not have the cash to purchase such check."

Now the Court held:

"We admit there is much force in this contention, and though we do not decide its merit, are puzzled why so drastic requirement is made when the giving of security would accomplish the desired purpose.

"We think, however, that appellant could have presented his contention of non-control under the Section cited *supra*, and that he failed to exhaust his administrative remedy by not so acting. If he there had prevailed, there would be no occasion to invoke the challenged provisions of 840.11."

That was decided by the Ninth Circuit on June 24, 1949, and I point that out to the Court, inasmuch as the defendant in this case had failed to avail her-

self of the administrative [67] remedy as set out in Procedural Regulation No. 2.

May I have that order, No. 4 I believe it is.

This order, your Honor, was issued when Procedural Regulation No. 1 was in effect. The order itself contains a provision requiring refund to the tenant, and says,

“Any rent collected from the effective date of this Order in excess of the amount provided in this Order shall be refunded to the tenant within 30 days from the date this Order is issued unless the refund is stayed in accordance with the provisions of Rent Procedural Regulation No. 1.”

The defendant failed to avail herself of those Rent Procedural Regulations providing for an appeal, and therefore at this time can not challenge the validity of this order.

Now, in the case of *Woods vs. Stone*, 68 Supreme Court, 624, the Court commented on the order to refund and the retroactive feature of the order, and this is what the Court said:

“Under the system of rent control as established, a landlord is required to register rented accommodations within thirty days after they are first devoted to that use. This brings notice to the control authority that the premises are within its official responsibility and provides data for quick, if tentative, determination [68] as to whether the rental exacted exceeds the level permitted by the policy of Congress set out in the statute.

“But when, as in this case, the landlord does not comply with this requirement, there is likelihood that, as happened here, his transaction will be overlooked for some time or perhaps escape scrutiny entirely. But the landlord is not allowed thus to profit from his own disobedience of the law. If he could keep the excess collections by thus retarding or preventing scrutiny of his contract, he would gain an advantage over all landlords who complied with the Act as well as over tenants whose necessity for shelter is too pressing to admit of bargaining over price. The plan therefore provides that, despite his failure to register, the landlord may continue to collect his unapproved price, but only on condition that it is subject to revision by the public authority and to a refund of anything then found to have been excessive.”

That was the decision of the Supreme Court in the case of Woods vs. Stone.

Now, your Honor, getting back to the facts in this case, there is no question but this unit was rented as an entirety to the members of one family, consisting of Mr. Lynch, Mrs. Lynch, and her 16-year-old daughter. [69]

The evidence shows—and this is admitted by Mrs. Sharp—that the Lynches paid for the utilities as the utilities were billed on a meter. That is unusual where a tenant rents a room in a rooming house. A tenant renting a room in a rooming house is furnished with utilities, and doesn't have to pay for whatever the meter shows.

There is no evidence in this case, your Honor, that any people other than the Lynches occupied the apartment; and it is our contention it was rented to them as an entire unit, and subject to the Housing Regulation, and subject to the maximum rent established by the order decreasing the rent and requiring refund to the tenant. Therefore, we submit judgment should be for the plaintiff as prayed for in the complaint.

Mr. Matot: Let me say one thing, if I may.

The Court: Will you wait a minute. I want to ask counsel a question, if I may.

Mr. Scheir: Yes, I will be glad to answer.

The Court: Supposing this was a new building and had never been rented at all until the date of this lease: Would they have to file a registration?

Mr. Scheir: I will have to check the regulation, your Honor.

The Court: Under the law, aren't new buildings exempt?

Mr. Scheir: New construction, yes, completed after, I [70] believe it is, February 1, 1947.

The Court: Well, suppose this wasn't a new construction? Suppose this was an old construction, and had never been rented at all?

Mr. Scheir: It would have to be registered, your Honor.

The Court: It would have to be registered?

Mr. Scheir: Yes. Under the Regulation, certain accommodations are exempt, and among the exempt accommodations are those consisting of new construction built after February 1, 1947. On housing



accommodations, even though they had never been rented and were occupied by the landlord up to the day of this lease, the maximum rent—I will read this section:

“For controlled housing accommodations first rented on or after July 1, 1947,”——

And this renting took place in June,——

The Court: What is your citation?

Mr. Scheir: 825.4(c) of the Housing Regulation.

“——the maximum rent shall be the first rent for such accommodations. Within 30 days after so renting, the landlord shall register the accommodations as provided in Section 825.7. The Expediter may order a decrease in the maximum rent as provided in Section 825.5(c) (1) and (6).”

That takes care of housing accommodations which were never [71] rented prior to July 1, 1947, but which were in existence before that date,—February of 1947.

The Court: All right. Mr. Matot?

Mr. Matot: That argument is all right, your Honor, as far as it goes, but it doesn't go far enough, for this reason: This property was registered. It was registered over five years ago, as rooms. It was registered. Those cases have to do with property where there has been no registration filed. We are registered here.

That is the vice of the situation. If we had been guilty of failing to register, that would have been one thing; but no, we registered, and we gave a

lease for less money than we could have done under the registration, and I think we are entitled to the protection of the Court.

The Court: Well, I thought this was a rather simple case, that is, until this afternoon, when you have injected another theory into the case. So before making the decision, I want to read some authorities.

I will take the matter under submission.

Mr. Matot: Thank you, your Honor. I told you there was a serious question of law here.

The Court: I don't know, it may be serious. We will see.

Mr. Matot: I hope your Honor will keep in mind we have two adverse orders in this property.

The Court: I will keep all this in mind.

Mr. Scheir: I wondered if we were going to cite some more cases, because if we are I would like to cite a case.

The Court: If you have any cases that apply, you may do so.

Mr. Scheir: The case I have is Woods vs. Macken, decided by the United States Court of Appeals for the Fourth Circuit, No. 5941, decided December 19, 1949. I don't have the citation.

The Court: December 19, 1949?

Mr. Scheir: Yes.

The Court: And the name?

Mr. Scheir: Woods vs. Macken.

The Court: United States Supreme Court?

Mr. Scheir: United States Court of Appeals for the Fourth District.

I would like to point out to the Court that in the opinion there is a reference to an interpretation, and I think the reference covers the interpretation itself, so I don't have to submit it to you.

The Court: I will see if I can find the case.

Mr. Matot: That case doesn't apply to this situation. I have studied it thoroughly.

The Court: Mr. Matot, I will read the case and decide whether it does. [73]

Mr. Matot: I know, your Honor.

The Court: We will stand adjourned.

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### Certificate

I hereby certify that I am a duly appointed, qualified and acting official court reporter of the United States District Court for the Southern District of California.

I further certify that the foregoing is a true and correct transcript of the proceedings had in the above-entitled cause on the date or dates specified therein, and that said transcript is a true and correct transcription of my stenographic notes.

Dated at Fresno, California, this 27th day of July, A.D. 1950.

/s/ FRANCES D. BUCK,  
Official Reporter.

[Endorsed]: Filed August 1, 1950.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the United States District Court for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 43, inclusive, contain the original Complaint; Answer; Plaintiff's Request for Admissions; Answer to Request for Admissions; Memorandum of Opinion and Order for Judgment; Amended Findings of Fact and Conclusions of Law; Judgment; Notice of Appeal, Statement of Points on Appeal and Designation of Record on Appeal which, together with copy of Reporter's Transcript of proceedings on February 25, 1950, and original plaintiff's exhibits 1 to 9, inclusive, and original defendant's exhibit A, transmitted herewith, constitute the transcript of record on appeal to the United States Court of Appeals for the Ninth Circuit.

Witness my hand and the seal of said District Court this 1st day of August, A.D. 1950.

EDMUND L. SMITH,  
Clerk.

[Seal] By /s/ THEODORE HOCKE,  
Chief Deputy.



[Endorsed]: No. 12634. United States Court of Appeals for the Ninth Circuit. United States of America, Appellant, vs. Dorothy Sharp, Appellee. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed August 3, 1950.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.

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In the United States Court of Appeals  
for the Ninth Circuit

No. 12634

STATEMENT OF POINTS ON APPEAL  
UNITED STATES OF AMERICA,  
Plaintiff-Appellant,  
vs.

DOROTHY SHARP, DOES I TO X,  
Defendant-Appellee.

The following are the points upon which the appellant intends to rely upon appeal:

1. The Court below erred in finding that the maximum rent was approximately Ninety Dollars (\$90.00) per month and not Thirty Seven Dollars and Fifty Cents (\$37.50) as established by order of the Area Rent Director.

2. The Court below erred in failing to give full

force and effect to the order of the Area Rent Director establishing the maximum rent.

3. The Court below erred in finding that the previous maximum rent established under the rooming house regulation could not be and was not changed by order of the Area Rent Director.

4. The Court below erred in failing to accept the validity of the order of the Area Rent Director in the absence of proof that the defendant had exhausted her administrative remedies.

5. The Court below erred in failing to enter judgment for the overcharge which the defendant collected as a cleaning charge and for the use of a bed.

6. The Court below erred in failing to find that the plaintiff had established the overcharges by substantial evidence.

7. The Court below erred in refusing to enter judgment in favor of the plaintiff as prayed for in the Complaint.

Dated this 9th day of August, 1950.

/s/ FRANCIS X. RILEY,  
Attorney for Appellant.

[Endorsed]: Filed August 16, 1950.

[Title of Court of Appeals and Cause.]

APPELLANT'S DESIGNATION OF RECORD

Appellant, United States of America, hereby designates the following portions of the record to be printed on appeal:

1. Complaint filed July 15, 1949.
2. Answer filed January 4, 1950.
3. Plaintiff's Requests For Admissions filed January 16, 1950.
4. Defendant's Answer to Plaintiff's Request for Admissions filed January 25, 1950.
5. Memorandum Opinion and Judgment Order filed March 16, 1950.
6. Amended Findings of Fact and Conclusions of Law filed May 10, 1950.
7. Final Judgment entered May 10, 1950.
8. Transcript of Testimony.
9. Plaintiff's Exhibits 1 to 9.
10. Defendant's Exhibit A.
11. Notice of Appeal filed July 6, 1950.
12. Statement of Points relied on.
13. This designation.

Dated this 9th day of August, 1950.

/s/ FRANCIS X. RILEY,  
Attorney for Appellant.

[Endorsed]: Filed August 16, 1950.







**In the United States Court of Appeals  
for the Ninth Circuit**

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UNITED STATES OF AMERICA, *Appellant*

v.

DOROTHY SHARP, *Appellee*

---

**Appeal from the United States District Court for the Southern District  
of California, Central Division**

---

**BRIEF OF APPELLANT**

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ED DUPREE,  
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LEON J. LIBEU,  
*Assistant General Counsel*

FRANCIS X. RILEY,  
*Special Litigation Attorney*  
Office of the Housing Expediter  
Washington 25, D. C.

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# In the United States Court of Appeals for the Ninth Circuit

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No. 12634

UNITED STATES OF AMERICA, *Appellant*

v.

DOROTHY SHARP, *Appellee*

---

Appeal from the United States District Court for the Southern District  
of California, Central Division

---

## BRIEF OF APPELLANT

---

### STATEMENT OF JURISDICTION

The appellant, the plaintiff below, appeals from a final judgment of the United States District Court for the Southern District of California, Central Division, denying a prayer for treble damages, an injunction and restitution for rent overcharges pursuant to Sections 205 and 206(a) and (b) of the Housing and Rent Act of 1947, as amended (50 U.S.C.A. 1881, et seq.) (R. 30). The judgment was entered on May 10, 1950 (R. 30). Notice of Appeal was filed on July 6, 1950 (R. 31). Jurisdiction of this Court is conferred by Section 1291 of the Judicial Code (28 U.S.C.A. 1291).

**STATEMENT OF THE CASE**

The United States filed suit against the defendant for overcharges of rent at 430 Daisy Avenue and 537 Melrose Way, Long Beach, California (R. 2). The overcharge at 430 Daisy Avenue resulted from the defendant's registration of the premises in 1946 as individual rooms in a rooming house (Plaintiff's Exhibit 9) (R. 89), and then subsequently renting the premises on June 11, 1948 as a single housing accommodation (a furnished apartment) for the first time (R. 56).

In January 1949, the defendant was called into the Area Rent Office and was told that she must file a registration statement covering the premises rented as an entire unit (R. 73). She did file a registration statement (Plaintiff's Exhibit 3, R. 41), and, according to her Answer, because she was "compelled" to do so "by threat and intimidations" (R. 9). The registration statement on its face shows that the rent collected was \$75.00 per month for the entire unit as represented in the written lease between the parties (R. 56). On March 23, 1949, the Area Rent Director issued an order reducing the maximum rent on the entire unit to \$37.50 per month effective from the date of the lease, June 11, 1948 (Pl. Exh. 4—R. 44).

The violations at 537 Melrose Way occurred because the defendant charged a dollar extra for the use of the bed and \$5.00 extra as a cleaning charge (R. 24), without permission of the Expediter.

The case went to trial on February 25, 1950 (Honorable Harry C. Westover, D.J. sitting) (R. 32). The trial developed the facts as set forth above and at its conclusion, the Court below entered Findings of Fact

and Conclusions of Law (R. 24), which included a Memorandum Opinion of the Court (R. 20). Based upon its Findings and Memorandum Opinion, a judgment was entered for the defendant (R. 30).

In its Findings of Fact, the Court below found that the accommodations in question were subject to the Act of 1947 (No. 1, R. 125); that the defendant did not receive rent in excess of the maximum (No. 2, R. 25); that the defendant did not collect more than the legal maximum on either housing accommodation (No. 3 to 5, R. 26); that the premises at 430 Daisy Avenue were registered on August 14, 1946 "as a rooming house, of four individual furnished rooms" (No. 7, R. 27); that the defendant rented the entire premises as a unit on June 11, 1948 for \$75.00 per month (No. 8, R. 27); that the said premises "had never been rented or registered" as a unit (No. 9, R. 27); that an order has never been entered altering the registered rent on the individual rooms (No. 10, R. 27); that an order was issued on March 23, 1949 reducing the rent on the premises in question from \$75.00 to \$37.50 per month (No. 11, R. 27); that the registration filed on January 14, 1949 was "a new registration and not a modification of the previous one" (No. 13, R. 28); that the entire premises rented under the written lease covered the individual units previously registered on August 14, 1946 (No. 15 and 16, R. 28); and that 430 Daisy Avenue was rented as a single unit for the first time on June 11, 1948 (No. 19, R. 29). As a conclusion of law, the Court held that the United States was not entitled to a judgment against the defendant (R. 29).



In its Memorandum Opinion, which was adopted as further Findings of Fact (No. 20, R. 29), the Court below found that the premises “had been rented as individual furnished rooms” (R. 21). After renting the premises as an entire unit, the Expediter maintained that another registration was required (R. 21). The Court then said that notice was not served upon the defendant stating the grounds upon which the Area Rent Office intended to reduce the rent, that the only evidence before the Court was that the Order had been entered “upon the initiative of the Housing Expediter, and no reasons were given to the landlord for the proposed change” (R. 22). The Court further found that the premises in question were “controlled housing accommodations” and had been registered as rooms and the rooming house registration was a valid existing one which the Expediter could have modified (R. 22). The Court then questioned the right of the Expediter to demand a new registration based upon the renting of the premises as an entire unit (R. 22). The Court further found that the defendant had complied with the law by registering the premises originally on August 14, 1946 (R. 23) and then cited Section 203(a) of the Act (*Infra*, p. 10) as authority for the conclusion that the Expediter had no authority to establish a maximum rent pursuant to the Emergency Price Control Act of 1942 (R. 23). The Court then concluded that the Expediter had no authority to require the registration statement and had no authority to issue an order reducing the rent to \$37.50 (R. 24).

With regard to the accommodation at 537 Melrose Way, the Court found that although \$6.00 had been



collected in excess of the maximum rent, that the tenant had received the *quid pro quo* and, therefore, “there is no overcharge as to Unit 537” (R. 24).

From the judgment denying plaintiff’s prayer, the Government appeals (R. 31).

### SUMMARY

The Government relies upon three grounds for reversal of the judgment of the Court below:

*First*, the Court below erred in failing to give full force and effect to the order of the Area Rent Director, because:

a) The Expediter has authority pursuant to the Act of 1947, to establish maximum rents, and,

b) The defendant’s failure to exhaust her administrative remedies precludes a challenge to the validity of the order establishing the maximum rent.

*Second*, the Court below should have entered a judgment for the Government, after having found that excess collections had been made, even though additional services had been rendered, but without application to the Expediter for an increase in rent, or the issuance of an order increasing the legal rent.

*Third*, the Court below found rents in excess of those established had been collected, but denied recovery on the ground that the Area Rent Director had no authority to establish those rents. Therefore, the findings of the Court are “clearly erroneous” and should be reversed.

## ARGUMENT

## I.

**The Court Below Erred in Failing to Give Full Force and Effect to the Order Issued by the Area Rent Director Reducing the Maximum Rent on the Premises in Question.**

As stated above, the basic facts in this case are not in dispute. The defendant registered her housing accommodations at 430 Daisy Ave., Long Beach, on August 14, 1946, "as a rooming house, of four individual furnished rooms" (Finding 7, R. 27; See, Pl's Exh. 9). The aggregate ceiling rent on the premises was "approximately \$90.00 per month" (id.) On June 11, 1948, the defendant under written lease rented the entire premises at 430 Daisy Ave., as a complete housing unit (R. 56). Subsequently, (January 14, 1949), the defendant filed a registration statement on the premises, registering it under the housing regulation as a unit (Pl's Ex. 3—R. 41),<sup>1</sup> at a rental of \$75.00 per month. The Area Rent Director issued an order on March 23, 1949, reducing the rent to \$37.50 per month, effective to the date of the lease, June 11, 1948, and ordering a refund of the excess collected (R. 44). No protest was filed nor appeal taken from the issuance of that order (R. 77). The Court below, however, refused to give effect whatever to this order, on the ground that, "the Office of Housing Expediter had \* \* \* no authority to make the order reducing the rent from \$75.00 to \$37.50" (R. 24). The Court seemed to base this conclusion on the ground that the Expediter lacked authority to issue an order establishing a maximum rent on

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<sup>1</sup> In her answer she pleads that she was "compelled" to sign this registration, by "threat and intimidations" (R. 9).

any property controlled under the Emergency Price Control Act of 1942, as amended (50 U.S.C.A. 901, et seq.) (R. 23).

The Court below was in error in reaching the conclusion that the order was invalid, because (1) The Expediter does have authority to establish rents pursuant to the Act of 1947; and (2) the order was valid in the Court below inasmuch as the defendant failed to exhaust her administrative remedies. These contentions will be discussed in order.

**1. The Expediter has authority to establish maximum rents pursuant to the Act of 1947.**

Preliminary to the discussion of the main point, the question of registering housing accommodations must be clarified. The Court below concluded that the registration of the individual rooms in the rooming house, sufficiently covered the rental of housing accommodations as an entire unit (R. 22). That is, that the maximum rent for the entire unit, when rented as such, was the aggregate of the rents on the individual rooms (R. 23). The regulations are to the contrary.

There are two regulations in issue here. The first is the Rent Regulation for Transient Hotels, Residential Hotels, Rooming Houses and Motor Courts (8 F.R. 7334).<sup>2</sup> The second is the Controlled Housing Rent Regulation (12 F.R. 4331; 13 F.R. 1861; 14 F.R. 1571). The former regulation provided that "This regulation

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<sup>2</sup> The defendant registered pursuant to the terms of this regulation. The control of rooming houses was continued under a similar regulation pursuant to the Act of 1947. See, Rent Regulation for Controlled Rooms in Rooming Houses and Other Establishments (12 F.R. 4302; 13 F.R. 1873; 14 F.R. 7334).

applies \* \* \* to all rooms in residential hotels, rooming houses \* \* \*” (Section 1; see full text, *infra*, p. 29). Further, the regulation provides in Section 1(b) :

“*Housing to which this regulation does not apply.*  
This regulation does not apply to the following:  
\* \* \*

(4) *Entire structures used as hotels, rooming houses or motor courts.* Entire structures or premises used as hotels, rooming houses or motor courts, as distinguished from the rooms within such hotels, rooming houses or motor courts”.

Therefore, by the express terms of the regulation, the only maximum rent established by the original renting, was that on the rooms themselves. Until rented as a unit, *the apartment itself did not have a maximum rent established.*

Conversely, the Housing Regulation exempts from its control all accommodations subject to the Rooming House Regulation (See, Section 1(b)(iii), *infra*, p. 26). It is common for a rooming house to have two registrations. One, covering the house itself; the other, covering the renting of the individual rooms. The two regulations complement one another, thereby securing for the landlords the most equitable results from two distinct types of operation. As was said by the Emergency Court of Appeals in *Bowman v. Bowles*, 140 F. 2d 974, at p. 978:

“\* \* \* Generally, we find that the Administrator, in exercising his delegated authority over rents, issued the Housing Regulation to provide control for



accommodations rented on monthly or longer terms and issued the Hotel Regulation to provide control over accommodations rented on daily, weekly or monthly terms. \* \* \* However, differences in the types of business covered by the two Regulations required variations in their provisions. One variance is that the Housing Regulation makes no provision for a sliding scale of rents, whereas such provision is included in the Hotel Regulation. The right to seek adjustments has been granted in the Housing Regulation when there is a substantial increase or decrease in the number of occupants, but this is obviously quite different from the provisions of the Hotel Regulation which permit, without need of seeking an adjustment, a maximum rental schedule for daily, weekly and monthly terms and for varying numbers of occupants. Other provisions of the Hotel Regulation, clearly applicable to a business based on short term occupancies, are those requiring that no tenant be required to change his term of occupancy and that landlords continue to offer for rent on a weekly or monthly term of occupancy the same number of rooms so rented in June, 1942. \* \* \*

The Court below erred, therefore, in failing to recognize that these two distinct operations made it imperative to have two registrations on this property, in order to establish two separate, legal rents. And the renting of the apartment as such was subject to a maximum rent totally distinct from the maximum rents established on the individual rooms comprising it.



We come then, to the question of whether the Expediter has authority to establish rents under authority of the Act of 1947. The Court below found that "The requirement of the Rent Control Act to register was originally met by the defendant because, on August 14, 1946, she had filed a registration \* \* \* and had the ceiling established on the rooms in the house" (R. 23). The Court then cited Section 203(a) of the Act,<sup>3</sup> and concluded it was unnecessary to register the rooms when rented as an apartment (R. 23). This action of the Court must be interpreted to mean that the rent having been established under the Act of 1942, no other action could have been taken to establish a rental on the entire unit under the later Act.

If the Court meant that the expeditor may not establish maximum rents under the Act of 1947, the legislative history fails to support the contention.

"Administration of present rent controls under authority of the Emergency Price Control Act of 1942, as amended, would terminate after the effective date of this title, which is the first day of the first calendar month following the month in which the bill is enacted into law. Thereafter, rent controls would be exercised under the provisions of this title and administered by the head of such established department or agency of the Government

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<sup>3</sup> That Section of the 1947 Act provides:

"Sec. 203(a) After the effective date of this title, no maximum rents shall be established or maintained under the authority of the Emergency Price Control Act of 1942, as amended, with respect to any housing accommodations."

as the President designates, \* \* \*.” (H. Rep. 317, 80th Cong. 1st Sess.—p. 12)

Furthermore, the language of the Act gives the Expediter authority “to issue such regulations and orders, \* \* \*, as he may deem necessary to carry out the provisions [of Section 204]”,<sup>4</sup> (Section 204(d), *infra*, p. 25) which is the Section of the Act providing for the control of rents.<sup>5</sup>

If the Court below intended to hold that rents once established under the Act of 1942, may not have rents set under the Act of 1947, the language of the Act fails to support it. The premises here were first rented in 1948 as an entire unit. Of necessity, therefore, the rent had to be established under the existing Act and the regulations issued pursuant thereto. Even if a rent had been established pursuant to the Act of 1942, nothing in the present Act prevented the Expediter from acting under the present law.

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<sup>4</sup> Section 204(a) reads in full:

“Sec. 204. (a) The Housing Expediter shall administer the powers, functions, and duties under this title; and for the purpose of exercising such powers, functions, and duties, and the powers, functions, and duties granted to or imposed upon the Housing Expediter by title I of this Act, the Office of Housing Expediter is hereby extended until the close of June 30, 1951.”

<sup>5</sup> Section 825.4(a) of the regulation provides:

“The maximum rent for any housing accommodation under 825.1 to 825.12 inclusive, (unless and until changed by the Expediter as provided in 825.5), shall be the maximum rent which was in effect on June 30, 1947, as established under the Emergency Price Control Act of 1942, as amended \* \* \*.” See Section 206(a) of the Act, *infra*, p. 17.

Section 4(c) of the present Regulation (issued pursuant to Section 204(d)) (*infra*, p. 25) controls the present situation. "For controlled housing accommodations first rented on or after July 1, 1947, the maximum rent shall be the first rent for such accommodations." The premises, however, must be registered within thirty days, and the Expediter may decrease that rent by order, on the ground that rent is higher than generally prevailing, or that the first rent was made at an abnormally high seasonal period.<sup>6</sup> Since this regulation is not an irrational administrative construction of Section 204(d) it is binding on the courts. *Porter v. Crawford & Doherty*, 154 F. 2d 431, 433 (C.A. 9th).

Thus, the Expediter both under the Act and by the provisions of his regulation had the authority to establish a legal maximum rent on the premises in question, when rented as a furnished apartment.

**2. The order was valid in the Court below since the defendant never exhausted her administrative remedies.**

The Court below incorrectly held that the order issued reducing defendant's rent was invalid, because "no notice was served upon the defendant stating the proposed action or the grounds therefor" (R. 21).<sup>7</sup> In

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<sup>6</sup> The Text of Sections 4(e), 5(c)(1) and (6) appear, *infra*, pp. 27-28.

<sup>7</sup> The Court here cited 840.7 of the Regulation which provides in pertinent part:

" 'In any case where the Rent Area Director . . . deems it necessary or appropriate to enter an order on his own initiative he shall, before taking such action, serve a notice on the landlord of the housing accommodations involved, stating the proposed action and the grounds therefor.' "

so ruling the Court below erred because this conclusion is not only unfounded, but it is directly contrary to the evidence. Plaintiff's Exhibit No. 4 (See, *infra*, p. 31) clearly shows on its face that the defendant was not only notified prior to the issuance of the order of March 23, 1949, but that she objected to its issuance in writing on "3/9/49".

In any event, the validity of the order issued could not be raised by way of defense, in the absence of an exhaustion of administrative remedies. There is no question here that defendant failed to exhaust her remedies, in the light of her testimony that she was compelled by the regulation to deposit the amount of the refund, before her appeal could be filed and she "didn't have the money to deposit"<sup>8</sup> (R. 77).

In deciding that the order in issue was invalid even though the defendant had not exhausted her administrative remedies, the Court below nullified "the long settled rule of judicial administration that no one is entitled to judicial relief for a supposed or threatened injury until the prescribed administrative remedy has been exhausted." *Myers v. Bethlehem Corp.*, 303 U. S. 41, 51. It is axiomatic that the foregoing rule applies where the one injured is the moving party in equity. *Aircraft & Diesel Corp. v. Hirsch*, 331 U. S. 752; *McCauley v. Waterman S. S. Corp.*, 327 U. S. 540; *Bab-*

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<sup>8</sup> The refund amounted to \$300.00.

Section 840.16 of Procedural Regulation No. 1 (13 F.R. 2369) provided that the refund provisions of an order shall be stayed pending appeal, if "a certified check or a money order in the amount of the refund \* \* \*" accompanies an appeal within 30 days of the issuance of the order (*Infra*, p. 28). See, *Babcock v. Koepke*, 175 F. 2d 923 (C.A. 9th).



*cock v. Koepke*, 175 F. 2d 923 (C. A. 9th) ; *Anderson v. Schwellenbach*, 70 F. Supp. 14 (N. D. Cal.), 3-Judge Court.

The rule applies with equal force where the party against whom the enforcement action is filed attacks the validity of the order by way of defense.

This Court has consistently applied that rule. In *United States v. La Verne Co-op Citrus Assn.*, 143 F. 2d 415 (C. A. 9th), the Government sought an injunction restraining defendants from handling lemons in violation of an order of the Secretary of Agriculture. The District Court refused to permit evidence on the question of the constitutionality of the order, on the ground that the Act<sup>9</sup> provided for an administrative remedy, which had not been exhausted by the defendants. The injunction issued and the defendants appealed. In affirming that judgment, this Court held that an administrative remedy must be pursued to completion before invoking equity jurisdiction, whether the party affected is plaintiff or defendant.

“The question then arises whether the administrative remedy rule applies where the one harmed by the administrative order is the defending party in the equity action. The doctrines of primary jurisdiction and of administrative finality are equally persuasive where the issue is raised by defending parties as where it is raised by moving parties. A consideration of the defense in an enforcement action would nullify the uniformity

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<sup>9</sup> Agricultural Marketing Agreement Act of 1937 (7 U.S.C.A. 601 *et seq.*)



achieved by devising a single procedure for testing orders promulgated in accordance with the terms of the Act. \* \* \*” (at p. 420)

This decision was made in the light of the Supreme Court’s ruling in *Yakus v. United States*, 321 U. S. 414. There the Court answered the sole question “whether the validity of a regulation may be challenged in defense of a prosecution for its violation although it had not been tested by the prescribed administrative procedure \* \* \*” (id. p. 419). In holding that the validity of an order may not be challenged, even in a criminal prosecution, where the record shows that the administrative process has not been used, the Court said, at p. 434:

“\* \* \* petitioners have failed to seek the administrative remedy and the statutory review which were open to them and that they have not shown that had they done so any of the consequences which they apprehend would have ensued to any extent whatever, or if they should, that the statute withholds judicial remedies adequate to protect petitioners’ rights.”

See too, *Woods v. Durr*, 176 F. 2d 273 (C. A. 3rd).

So, here, where the record is conclusive that the defendant has failed to follow the administrative procedure, she may not now resort to the Court for relief. To do so would nullify “the long settled rule” of exhaustion of administrative remedies and permit courts to exercise jurisdiction which established principles

now deny them<sup>10</sup> at the threshold of the proceedings.

Thus, the Court below erred on two grounds in finding that the order was invalid because of a denial of procedural due process; (1) The order on its face shows that a written objection to its issuance was received and considered, two weeks prior to issuance; and (2) she failed to appeal the order and thus, exhaust her administrative remedies, which are conditions precedent to judicial review either by bill in equity or by way of defense.

## II.

### **The Court Below Erred in Failing to Enter a Judgment Against the Defendant on the Premises at 537 Melrose Way, After Finding That the Overcharge Had Been Collected.**

The Court below found as a fact that the premises at 537 Melrose Way were controlled housing accommodations, and as such were subject to the Act and the regulations (No. I, R. 25). In its oral opinion (adopted as a Finding of Fact, No. XX—R. 29), the Court found the overcharge had been collected, but the receipt showed additional services had been rendered, and, “There is nothing in the case to indicate that the tenant was entitled to an additional bed without paying therefor nor was entitled to the cleaning of her apartment free of charge; consequently the Court is of the opinion that there is no overcharge as to Unit 537” (R. 24). Under this decision a landlord may collect more than the legal maximum “in connection with the use and occupancy of any housing accommodation”, and, if the

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<sup>10</sup> There is, of course, no question here of denial of due process, since the defendant failed to take the initial steps invoking it.

*quid pro quo* is furnished, no overcharge results. Such a conclusion could successfully nullify effective rent control.

The Act, the regulation and the reported decisions are contrary to this holding of the Court below. Section 206(a) of the Act<sup>11</sup> forbids the collection of rent in excess of the maximum established by it, or any regulation,<sup>12</sup> or order, of the Expediter. In addition, the regulation specifically authorizes a landlord to obtain rent increases in an orderly, legal manner with the prior approval of the Expediter. Concomitantly, it provides an effective measure of protection to the tenant from unjustified and unnecessarily burdensome in-

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<sup>11</sup> That Section reads as follows:

“Sec. 206. (a) It shall be unlawful for any person to demand, accept, or receive any rent for the use or occupancy of any controlled housing accommodations in excess of the maximum rent prescribed under section 204, or otherwise to do or omit to do any act, in violation of this Act, or of any regulation or order or requirement under this Act, or to offer, solicit, attempt, or agree to do any of the foregoing.”

<sup>12</sup> Section 2(a) of the Regulation provides:

“(a) *General prohibition.* Regardless of any contract, agreement, lease, or other obligation heretofore or hereafter entered into, no person shall offer, demand or receive any rent for or in connection with the use or occupancy on and after the effective date of §§ 825.1 to 825.12, inclusive, of any housing accommodations within the Defense-Rental Area higher than the maximum rents provided by §§ 825.1 to 825.12, inclusive; and no person shall offer, solicit, attempt, or agree to do any of the foregoing. A reduction in the services, furniture, furnishings, or equipment required under § 825.3 shall constitute an acceptance of rent higher than the maximum rent. Lower rents than those provided by §§ 825.1 to 825.12, inclusive, may be demanded or received.”

creases.<sup>13</sup> The wisdom of this provision has been recognized and applied by several Courts of Appeal.

In *Creedon v. Olinger*, 170 F. 2d 895 (C. A. 5th), the District Court denied recovery for overcharges "for the reason that refrigerators had been furnished by some of the tenants, air-conditioning had been made possible by the defendant to others, and at times during the period in question relatives and friends had visited certain of the tenants and during the visit occupied apartments with them" (id. p. 897). The District Court held that:

" 'It is the business of the courts to try to discover the just way and from an impartial attitude to see where the right is.' " (id.)

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<sup>13</sup> Section 5(a)(3) of the Regulation says:

"(a) *Grounds for increase of maximum rent.* Any landlord may file a petition for adjustment to increase the maximum rent otherwise allowable only on the grounds that: \* \* \*

(3) *Substantial increase in space, services, furniture, furnishings or equipment.* There has been a substantial increase in the services, furniture, furnishings, or equipment provided with the housing accommodations since the date or order determining its maximum rent or a substantial increase in the living space since June 30, 1947 but before April 1, 1948. No increase in the maximum rent shall be ordered on the ground set forth in this paragraph (a)(3) unless the increase in living space, services, furniture, furnishings or equipment occurred with the consent of the tenant or while the accommodations were vacant: *Provided*, That an adjustment may be ordered, although the tenant refuses to consent to the increase in living space, services, furniture, furnishings or equipment, if the Expediter finds that such increase (i) is reasonably required for the operation of a multiple dwelling structure or other structure of which the accommodations are a part or (ii) is necessary for the preservation or maintenance of the accommodations."



In reversing that decision the Court of Appeals held that the landlord's relief was in the administrative procedure provided, and not in the courts. The Court then concluded:

“Since the undisputed evidence clearly discloses overcharges during the period alleged in the complaint, judgment for at least the amount of the overcharges must be granted in favor of the Expediter or, by way of restitution, to the tenant.” (id.)

A more exaggerated case came before the Court of Appeals for the First Circuit in *Elma Realty Co. v. Woods*, 169 F. 2d 172. There the appellant's building was burned in part, rendering it unfit for human habitation. The Area Rent Director reduced the rent to \$1.00 per week “due to substantial deterioration”, but informed the appellant that it would increase the rent when made habitable again. On June 6, 1947, after rehabilitation of the premises, the rents were adjusted upward. However, the appellant had been collecting increased rent from the previous April without authorization. This collection constituted the overcharge. In upholding the trial court's judgment of restitution and double damages, the Court said, at p. 174:

“\* \* \* Thus although the appellant was undoubtedly entitled to an upward adjustment of its maximum rents after its apartments were again habitable, nevertheless the regulations do not permit it to increase its rents until after it has ap-

plied for and obtained permission to do so. *Thierry v. Gilbert*, 1 Cir., 147 F. 2d 603.”

In *Woods v. Polis*, 180 F. 2d 4 (C. A. 3rd), the landlord raised the rent from \$50 to \$65 per month, but claimed “he waived some \$400 worth of repairs and obligations, the cost of which should have been borne by the lessees but which in fact were not” (*id.* p. 6). The District Court entered a judgment for treble damages and injunctive relief. The Court of Appeals affirmed the judgment, saying the landlord should have petitioned the Expediter for an adjustment of rent:

“However, even if there was a shifting in the obligations between the first and second arrangements by this landlord with his tenant, it is not disputed that there was no application made for a change in rent. The rent regulations permit the landlord to petition for an adjustment when there has been a substantial increase in services. That administrative procedure was open to the landlord here, but he chose instead to make his own determination of the worth of the services which were to be performed by the lessees under the freeze date lease. Such a determination is not binding upon the Housing Expediter. See *Elma Realty Co. v. Woods*, *infra*. The freeze date registration of the premises remained in full force, and it permitted a maximum rental of \$50 per month. It was unlawful for the landlord to receive more than \$50 per month in cash until he had successfully petitioned for an adjustment; any cash payment in excess of that amount was an overcharge which

could be recovered by the Expediter.” (id. pp. 6-7)

See, too, *Woods v. Dodge*, 170 F. 2d 761 (C. A. 1st); *McCormack v. Kovacevich*, 170 F. 2d 588 (C. A. 7th); *Kalwar v. McKinnon*, 152 F. 2d 263 (C. A. 1st); *Woods v. Kimmey*, 88 F. Supp. 838 (W. D. Pa.).

The decision of the Court below that although an additional charge was made, the tenant received additional services, is contrary to these well reasoned authorities. It is respectfully requested that this Court bring the decision of the Court below into accord with this overwhelming weight of authority.

### III.

#### **The Finding of the Court Below That the Plaintiff Failed to Establish the Overcharge Is Contrary to the Evidence and Is Clearly Erroneous.**

In finding that the defendant did not overcharge (Findings III and IV, R. 26), the Court below disregarded the admissions of the defendant and the conclusive proof in the record. The attack on these findings, therefore, is not contrary to the provisions of Rule 52(a) of the Federal Rules of Civil Procedure (28 U. S. C. A. foll. 723(c)),<sup>14</sup> since these findings are not supported by any evidence whatever in the record. They are, therefore, “clearly erroneous.” *Lerner Stores Corp. v. Lerner*, 162 F. 2d 160, 162 (C. A. 9). More-

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<sup>14</sup> Rule 52(a) provides in part as follows:

“\* \* \* Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses.

\* \* \*”

over, the record is conclusive that the Expediter proved both the maximum rent and the collection of rent in excess of the maximum.

1. As to the overcharge at 537 Melrose Way, the plaintiff introduced the order of the Area Rent Director, establishing the rent at \$29.00 per month (Plaintiff's Exhibit 2, R. 37). That Exhibit is uncontradicted in the record.<sup>15</sup> The tenant of that accommodation testified that she paid \$30.00 for one month and \$35.00 for the second month and that these amounts included extra charges for a bed and cleaning charge, respectively (R. 64). The receipts introduced into evidence (Plaintiff's Exhibit 8, R. 65), show on their face that these charges were collected for the additional services (R. 24). There is no contradiction in the record that these amounts were not received. There is merely the claim that the excess amount collected was not collected as rent (R. 7; Nos. 2, 3, 4 (R.16)). In other words, it was defendant's sole defense that these amounts, if collected, were collected not as rent but as payments for additional services. However, it is conclusive that since these charges were made "in connection with the use and occupancy of the housing accommodations", the

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<sup>15</sup> The accommodation here is "a small apartment that faces the side street, \* \* \*", and is "a different building" (R. 84). There is no question, therefore, that this is in any way covered by the original registration statement at 430 Daisy Ave. (P. Ex. 9—R. 89). Defendant's claim that the legal rent was "\$95.00 per month" (No. 7—R. 17) is completely without support in the record.



amounts collected were rent.<sup>16</sup> (See, *Woods v. Dodge*, 170 F. 2d 761 (C. A. 1st)).

It follows, therefore, that since the plaintiff established the maximum rent without contradiction in the record and since the sole testimony in the record, supported by exhibits, is to the effect that more than the maximum rent was paid and since the Court below found that these collections were made, it was error not to enter a judgment for the amount of the overcharge. *Fontes v. Porter*, 156 F. 2d 956 (C. A. 9); *Bowles v. Glick Bros. Lumber Co.*, 146 F. 2d 566 (C. A. 9); *Woods v. Haydell*, 178 F. 2d 914 (C. A. 5); *Bowles v. Hastings*, 146 F. 2d 94 (C. A. 5).

2. The plaintiff proved the maximum rents on the property located at 430 Daisy Avenue with the introduction of the order of the Area Rent Director (Plaintiff's Exhibit 4 (R. 44)). The overcharge was established by the admission of the defendant that she collected \$75.00 per month (R. 9). It is further established by plaintiff's Exhibit 6 (R. 56) and by the Court's Finding of Fact that \$75.00 per month was collected for the period mentioned in plaintiff's Complaint (No. 8, R. 27). Thus, the evidence is substantial that the maximum rent for the premises was \$37.50 per month. It was uncontradicted that the defendant collected \$75.00 per month for the premises. Consequently, it was error for the Court below to fail to enter

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<sup>16</sup> Section 202(e) of the Act defines rent as:

“The term ‘rent’ means the consideration, including any bonus, benefit, or gratuity demanded or received for or in connection with the use or occupancy of housing accommodations, or the transfer of a lease of housing accommodations.”

a judgment for the plaintiff for at least the amount of the overcharge. *Fontes v. Porter, supra.*

#### CONCLUSION

It is respectfully submitted that the Court below erred in failing to enter a judgment for the plaintiff as prayed in the Complaint and that the judgment should be reversed with directions to the Court below to enter a judgment for the plaintiff as prayed.

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## APPENDIX

Housing and Rent Act of 1947, as amended (50 U. S. C. A., 1881, et seq.):

SEC. 204. (d) The Housing Expediter is authorized to issue such regulations and orders, consistent with the provisions of this title, as he may deem necessary to carry out the provisions of this section and section 202 (c).

## RECOVERY OF DAMAGES

SEC. 205. Any person who demands, accepts, or receives any payment of rent in excess of the maximum rent prescribed under section 204 shall be liable to the person from whom he demands, accepts, or receives such payment (or shall be liable to the United States as hereinafter provided), for reasonable attorney's fees and costs as determined by the court, plus liquidated damages in the amounts of (1) \$50, or (2) three times the amount by which the payment or payments demanded, accepted, or received exceed the maximum rent which could lawfully be demanded, accepted, or received, whichever in either case may be the greater amount: *Provided*, That the amount of such liquidated damages shall be the amount of the overcharge or overcharges if the defendant proves that the violation was neither willful nor the result of failure to take practicable precautions against the occurrence of the violation. Suit to recover such amount may be brought in any Federal, State, or Territorial court of competent jurisdiction within one year after the date of such violation: *Provided*,

That if the person from whom such payment is demanded, accepted, or received either fails to institute an action under this section within thirty days from the date of the occurrence of the violation or is not entitled for any reason to bring the action, the United States may institute such action within such one-year period. \* \* \*

SEC. 206. (b) Whenever in the judgment of the Housing Expediter any person has engaged or is about to engage in any acts or practices which constitute or will constitute a violation of any provision of this Act, or any regulation or order issued thereunder, the United States may make application to any Federal, State, or Territorial court of competent jurisdiction for an order enjoining such acts or practices, or for an order enforcing compliance with such provision, and upon a showing that such person has engaged or is about to engage in any such acts or practices a permanent or temporary injunction, restraining order, or other order shall be granted without bond.

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Controlled Housing Rent Regulation (12 F. R. 4331) :

“SEC. 825.1. (b) *Decontrolled and exempted housing to which §§ 825.1 to 825.12, inclusive, do not apply—*(1) *Exempted housing.* Sections 825.1 to 825.12, inclusive, do not apply to the following:

(iii) *Accommodations subject to the Rent Regulation for Controlled Rooms in Rooming Houses and other Establishments.* Rooms or other housing



accommodations subject to the provisions of Subpart B.”

§ 825.4. *Maximum rents*—(e) *Increase or decrease in space on or after April 1, 1948.* Where housing accommodations are changed on or after April 1, 1948, by a substantial increase or decrease in dwelling space, the maximum rent for the housing accommodations resulting from such change shall be the first rent charged after such change: *Provided, however,* That the Expediter at any time may order a decrease in the maximum rent as provided in §§ 825.5 (c) (1) and (6): *And provided further,* That the rent received for any rental period commencing on or after the date of the first renting shall be received subject to refund to the tenant of any amount in excess of the maximum rent which may later be fixed by an order under § 825.5 (c) (1) or (6) \* \* \*

“§ 825.5. (c) *Grounds for decrease of maximum rent.* The Expediter at any time, on his own initiative or on application of the tenant, may order a decrease of the maximum rent otherwise allowable only on the grounds that:

(1) *Rent higher than rents generally prevailing.* The maximum rent for housing accommodations established under paragraph (c), (d), (e), (g), or (j) of section 4 of the Rent Regulation for Housing, issued pursuant to the Emergency Price Control Act of 1942, as amended, or under § 825.4 (c) or (e) is higher than the rent generally prevailing in the defense-rental area for comparable

housing accommodations on the maximum rent date. \* \* \*

3 months after the date of filing of such registration statement.

\* \* \*

(6) *Seasonal rent.* The rent on the date determining the maximum rent was substantially higher than at other times of year by reason of seasonal demand or seasonal variations in the rent, for such housing accommodations. In such cases the Expediter's order may if he deems it advisable provide for different maximum rents for different periods of the calendar year.

---

Rent Proc. Reg. 1 (13 F. R. 2369):

SEC. 840.16. *Stay of landlord's obligation to refund.* (a) Where the Area Rent Director has entered an order under § 840.7, the effect of which is to require a landlord to make a refund to a tenant in accordance with the provisions of section 4 (c), 4 (e), 5 (b), (2), or 5 (c) (1) of the Controlled Housing Rent Regulation, section 5 (b) (2) of the Rent Regulation for Controlled Rooms in Rooming Houses, and Other Establishments, section 4 (c), 4 (e), 5 (b) (2), or 5 (c) (1) of the Controlled Housing Rent Regulation for New York City Defense-Rental Area, section 5 (b) (2) of the Rent Regulation for Controlled Rooms in Rooming Houses and Other Establishments in New York City Defense-Rental Area, section 4 (c), 4 (e), 5

(b) (2), or 5 (c) (1) of the Controlled Housing Rent Regulation for Miami Defense-Rental Area, section 5 (b) (2) of the rent regulation for Controlled Rooms in Rooming Houses and Other Establishments in the Miami Defense-Rental Area, or section 4 (c), 4 (e), 5 (b) (2), or 5 (c) (1) of the Controlled Housing Rent Regulation for Atlantic County Defense-Rental Area, the obligation to refund shall be stayed if the landlord within thirty (30) days after the date of issuance of said order, duly files an appeal from said order, together with a refund transmittal memorandum directed to the Regional Budget and Finance Officer on forms prescribed by the Housing Expediter accompanied by a certified check or money order in the amount of the refund payable to the United States Treasurer, and such additional information and documents as may be required. The money so deposited shall be distributed pursuant to the order of the Housing Expediter or in accordance with the final disposition of the proceedings.

---

Rent Regulation for Transient Hotels, Residential Hotels, Rooming Houses and Motor Courts (8 F. R. 7334):

“SECTION 1. *Scope of this regulation—*(a) *Rooms in hotels and rooming houses and Defense-Rental Area to which this regulation applies.* This regulation applies to all rooms in hotels and rooming houses within each of the defense-rental areas

and each of the portions of a defense-rental area (each of which is referred to hereinafter in this regulation as the 'Defense-Rental Area'), which are listed in Schedule A of this regulation, except as provided in paragraph (b) of this section.

In Schedule A, 'the maximum rent date' and 'the effective date of regulation' is given for each Defense-Rental Area listed. More than one effective date is given for different portions of a Defense-Rental Area where the same effective date is not applicable to the entire Defense-Rental Area. Wherever the words 'the maximum rent date' or the words 'the effective date of regulation' are referred to in this regulation, the dates given in Schedule A for the particular Defense-Rental Area or portion of the Defense-Rental Area in which the room is located shall apply. The effective date listed in Schedule A in each instance is the date rent regulation was effective in the particular Defense-Rental Area or portion of the Defense-Rental Area for rooms in hotels and rooming houses."



0-36  
17-7(47)

UNITED STATES OF AMERICA  
OFFICE OF THE HOUSING EXPEDITER  
OFFICE OF RENT CONTROL

STAMP OF ISSUING OFFICE

OFFICE OF HOUSING EXPEDITED

110 East Anaheim  
Long Beach 13, California

**ORDER DECREASING MAXIMUM RENT  
REQUIRING REFUND TO TENANT**

CONCERNING (ADDRESS OF ACCOMMODATIONS)

430 Daisy Ave., Long Beach, California

APARTMENT NO.

DOCKET NO.

99337-25A-b

TO: (Name and Address of Landlord)

Dorothy Sharp,  
428 Daisy Ave.,  
Long Beach, Calif.

The Rent Director, after consideration of all the evidence in this matter, has determined that the maximum rent for the above-described housing accommodations should be decreased on the grounds stated in Section (s)

5 C 1 of the Rent Regulation, and further for the reason (s) stated in Section (s)

5 C 1 of the Rent Regulation, the maximum rent so decreased and

terminated by this Order shall be effective from 6-11-48

Therefore, it is ordered that the maximum rent for the above-described accommodations be, and it hereby

decreased from \$ 75.00 per Month to \$ 37.50 per Month, effective

from 6-11-48. No rent in excess of \$ 37.50 Month (maximum rent established

by this Order) may be received or demanded.

Any rent collected from the effective date of this Order in excess of the amount provided in this Order

shall be refunded to the tenant within 30 days from the date this Order is issued unless the refund is stayed

in accordance with the provisions of Rent Procedural Regulation No. 1.

This Order is now in effect and will remain in effect until changed by the Office of the Housing Expediter.

LANDLORD'S LETTER DATED 3/9/49 HAS BEEN CONSIDERED.

ISSUED MAR 23 1949  
(Date)

*[Signature]*  
Rent Director

NOTICE TO LANDLORD AND TENANT: Read the reverse side of this order. RENT DIRECTOR FOR THE  
LOS ANGELES DEPARTMENT OF RENTALS

TO: (Name and Address of Tenant)

Mr. Tenant Occupant,  
430 Daisy Ave.,  
Long Beach, California

COMPLIANCE.

#22

09150300124 50



## NOTICE TO LANDLORD

This is a final **ORDER** which has been issued by the Rent Director decreasing the Maximum Rent for the accommodations described therein.

**THIS ORDER IS IMPORTANT—READ IT CAREFULLY.**—As of the date of issuance this Order establishes the Maximum Rent for both *future* and the *past* rental periods. Any rent in excess of the Maximum Rent, as finally fixed by this Order, which you have collected since the *effective date* of the Order, must be refunded to the tenant or tenants from whom it was collected.

The Rent Regulation provides that you must make these refunds to such tenants within 30 days from the date this Order is *issued* unless you obtain a stay of refund in accordance with Rent Procedural Regulation No. 1. The duty to make such refund is yours and you must make every effort to locate any prior tenants to whom a refund is due.

By taking the following steps you may comply with the Rent Regulation and this Order:

1. Do not collect rent in excess of the Maximum Rent fixed by this Order.
2. Make the required refunds within 30 days after the date this Order is issued, unless you obtain a stay of refund in accordance with Rent Procedural Regulation No. 1, above mentioned.

Failure on your part to make the refunds within the 30-day period above mentioned is a violation of the Rent Regulations and this Order and may subject you to suit for three times the amount refundable or \$50 whichever is greater.

## NOTICE TO TENANT

This is an Order issued by the Rent Director reducing the rent for the housing accommodations described herein. This Order establishes an effective date which is prior to the issuance date. This results in a reduction of the rent effective retroactively and the Order requires the landlord to refund to every tenant any rent paid by him in excess of the reduced rent for any rental period beginning on and after the effective date of the Order.

The Order is

1934

#4

tenant entitled thereto within 30 days in accordance with Rent Procedure

Case No. 9996-1460 vs. Sharp  
USA EXHIBIT # 4  
AS IDENTIFICATION  
 Date FEB 24 1950 No. 4 IN EVIDENCE  
 Date FEB 24 1950 No. 4  
 Clerk, U. S. District Court, Sou. Dist. of Calif.  
 Deputy Clerk

nt to the landlord for any period after the date of the Order (see Appendixes), and compare the rent you paid with the amount of refund due you for each rental period.

ing:

and has been stayed in accordance with





No. 12635

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

WESTERN AIR LINES, INC.,

*Petitioner,*

*vs.*

CIVIL AERONAUTICS BOARD,

*Respondent.*

---

On Petition for Review of an Order of the Civil Aeronautics  
Board

---

BRIEF OF PETITIONER, WESTERN AIR  
LINES, INC., IN SUPPORT OF PETITION  
FOR INTERLOCUTORY RELIEF.

---

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Los Angeles 14, California,  
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FILED

AUG 22 1951

PAUL R. ORRICK

CLERK



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WESTERN AIR LINES, INC.,

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---

BRIEF OF PETITIONER, WESTERN AIR  
LINES, INC., IN SUPPORT OF PETITION  
FOR INTERLOCUTORY RELIEF.

---

## I.

### OPENING STATEMENT.

The main issue on review is whether or not the Board erred in rejecting the petition of Western Air Lines, Inc., for an order consolidating seven proceedings pending before the Board.

The immediate issue is whether or not the Board should be enjoined from commencing, continuing and completing the seven proceedings pending determination of the review on its merits.

If this Court decline to issue an order staying the Board from taking further procedural steps in the proceedings, a favorable decision on review may prove to be hollow.

II.

**JURISDICTIONAL STATUTES INVOLVED.**

The right of review of the order here under scrutiny comes from Section 1006(a) of the Civil Aeronautics Act, which reads:

“Any order, affirmative or negative, issued by the Board under this Act, except any order in respect of any foreign air carrier subject to the approval of the President as provided in section 601 of this Act, shall be subject to review by the circuit courts of appeals of the United States or the United States Court of Appeals for the District of Columbia upon petition, filed within sixty days after the entry of such order, by any person disclosing a substantial interest in such order. After the expiration of said sixty days a petition may be filed only by leave of court upon a showing of reasonable grounds for failure to file the petition theretofore.” [49 U. S. Code 646(a).]

and from Section 10(a) of the Administrative Procedure Act, which reads:

“*Right of Review.*—Any person suffering legal wrong because of any agency action, or adversely affected or aggrieved by such action within the meaning of any relevant statute, shall be entitled to judicial review thereof.” [5 U. S. Code 1009(a).]

The right of this Court to issue a restraining order, in addition to its inherent power to protect its own proc-

esses, comes from Section 1006(d) of the Civil Aeronautics Act, which reads:

“Upon transmittal of the petition to the Board, the court shall have exclusive jurisdiction to affirm, modify, or set aside the order complained of, in whole or in part, and if need be, to order further proceedings by the Board. Upon good cause shown, interlocutory relief may be granted by stay of the order or by such mandatory or other relief as may be appropriate: Provided, That no interlocutory relief may be granted except upon at least five days’ notice to the Board.” [49 U. S. Code 646(d).]

and from Section 10(d) of the Administrative Procedure Act, which reads:

*“Interim Relief.*—Pending judicial review any agency is authorized, where it finds that justice so requires, to postpone the effective date of any action taken by it. Upon such conditions as may be required and to the extent necessary to prevent irreparable injury, every reviewing court (including every court to which a case may be taken on appeal from or upon application for certiorari or other writ to a reviewing court) is authorized to issue all necessary and appropriate process to postpone the effective date of any agency action or to preserve status or rights pending conclusion of the review proceedings.” [5 U. S. Code 1009(d).]



### III.

## STATEMENT OF THE CASE.

### A. Parties.

*Western Air Lines, Inc., Petitioner.* Western is the oldest American Flag airline, having commenced operations out of Los Angeles on April 17, 1926. It operates under permanent certificates of convenience and necessity from San Diego to Seattle via Los Angeles, San Francisco and Portland and between Los Angeles and Edmonton, Canada, via Las Vegas, Salt Lake City, Pocatello, Great Falls and other intermediate points. In addition, Western serves Ontario, Palm Springs, El Centro and Yuma in connection with an Imperial Valley operation. Western owns 98% of the outstanding shares of Inland Air Lines, Inc., which operates under permanent certificates of public convenience and necessity from Denver to Minneapolis—St. Paul via various intermediate points and between Denver and Great Falls (there linking with Western's main system) via various intermediate points. Western's system involves 3086 route miles and Inland's 1814. Western's executive offices are maintained in Los Angeles.

*Civil Aeronautics Board, Respondent.* The Civil Aeronautics Act, enacted in 1938, was designed to regulate civil aeronautics in a fashion somewhat comparable to the manner in which the Interstate Commerce Act regulates ground transportation. The Act set up a bipartisan agency designated the Civil Aeronautics Board, consisting of five members. This Board has power over civil aeronautics, including commercial air transportation, somewhat comparable to the power of the Interstate Commerce Commission over ground transportation.

*Southwest Airways Company, Intervener.* On May 22, 1946, in the *West Coast Case*,<sup>1</sup> the Board granted a temporary certificate to Southwest for a period of three years authorizing experimental feeder air service between Los Angeles and Medford, Oregon, involving 25 stations and approximately 1216 route miles. Southwest commenced operations on December 2, 1946. Although the three-year term expired on November 22, 1949, Southwest's temporary certificate will continue effective under Section 9(b) of the Administrative Procedure Act until final action of the Board in the *Southwest Renewal Case*.

Since May 22, 1946 the Board has authorized a number of important modifications in Southwest's certificate resulting in increasing its competitive stature with the trunklines.

*West Coast Airlines, Inc., Intervener.* In the *West Coast Case* a temporary three-year feeder certificate was granted to West Coast Airlines, Inc., between Medford, Oregon, and Bellingham, Washington, involving 21 stations with 688 route miles. West Coast commenced operation on December 5, 1946. Its certificate, by its term, was due to expire on November 22, 1949, but continues in effect under Section 9(b) of the Administrative Procedure Act in the same manner as Southwest's. Since it was granted, West Coast's certificate has been modified in similar fashion to that of Southwest's.

*Post Office Department.* Although not a formal party, the Post Office Department is a highly interested party. The fact that the Board *fixes* the air mail rates does not

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<sup>1</sup>Reported in Vol. 6 at page 961 of C. A. B. Reports. This was the third "set" of experimental feeder airlines certificated on a temporary basis. The first set was certificated on March 28, 1946, in the *Rocky Mountain States Case* (6 C. A. B. 695) and the second set on the same date in the *Florida Case* (6 C. A. B. 765).

diminish the interest of the Post Office in seeing that funds appropriated for postal service are not squandered in the guise of extravagant or needless mail pay. Usually, the Post Office Department is represented by counsel in proceedings before the Board directly concerning or indirectly influencing air mail rates. The obligation of the Postmaster General to pay the air mail rate fixed by the Board is found in Section 406(a) of the Act (49 U. S. Code 486).

### **B. The Order Under Review.**

On May 2, 1950 Western filed a petition (Appendix A) to consolidate in one proceeding for hearing and disposition seven separate proceedings then pending before the Board.

Two of the proceedings involve renewal of the three-year experimental feeder certificates of Southwest and West Coast for an additional five years. One concerns the proposed merger of Southwest and West Coast. Two more involve routes identical to the route that would exist if Southwest and West Coast were permitted to be merged, one of which is on behalf of Western to amend its permanent route between Los Angeles and Seattle to add additional intermediate points and the other is on behalf of Western Air Lines of the Pacific, Inc., which was organized by Western. These five constitute the core of the proceedings which Western sought to have consolidated.

Of the two remaining proceedings, one is the technical application of Western for approval of the acquisition of stock ownership of Western Air Lines of the Pacific, Inc.

The seventh proceeding sought to be consolidated is the *Reopened Additional California-Nevada Service Case*. It

was thought that the public interest would be served by including this in the consolidated proceedings as it concerns the extension of Southwest's temporary feeder route from Los Angeles to Phoenix by way of various intermediate points. Western is an applicant as well as an intervener in the *Reopened Additional California-Nevada Service Case*, and the routes involved in that proceeding are in no sense exclusive of the routes involved in the other five applications of concern here. No violence would be done to law or equity if the *Reopened Additional California-Nevada Case* were not consolidated with the others, although incongruous conclusions might be reached.

**(1) Effect of Southwest's Renewal Case Alone.**

The *Southwest Renewal Case* was initiated by the Board on April 4, 1949. Standing alone, it involved only a continuation for an additional five years of that which had been in operation for the past three and one-half years. It did not presage a new trunkline carrier directly competitive with Western on its coastal operations from San Diego to Seattle, as Southwest's northern terminal at Medford safely foreclosed that danger.

It would not have been sensible for Western to file an application which would have been mutually exclusive with the renewal of Southwest's temporary certificate. Southwest and West Coast conceded this in their answer to Western's petition to the Board for reconsideration when they noted on page 25:

"West Coast and Southwest are two separate companies with two separate and distinct operations. Western's applications are mutually exclusive with *neither* of them separately, and it is beyond Western's control to put them together for the purposes of attempting to obtain a mutually exclusive situation." (Emphasis included.)



The *Southwest Renewal Case*, still standing alone, involved a temporary feeder airline of only 1200 miles. It harbored no impending threat of creating a competitive problem which would be detrimental to the public interest and to Western.

**(2) Effect of West Coast's Renewal Case Alone.**

What has been said of the *Southwest Renewal Case* standing alone can be said to an even greater extent with respect to the *West Coast Renewal Case*. Continuation for an additional five years of a feeder system involving 700 miles with the southern terminal at Medford sounded no warning and gave no indication of the possibility of a violent alteration of the airline route structure in the Pacific Coast area.

Prior to April 10, 1950, when the *Merger Case* was filed, Western could not have filed a mutually exclusive application which would have been consolidated with the two separate *Renewal Cases*.

**(3) Effect of the Southwest-West Coast Merger Case.**

From January 1 through April 9, 1950 there were a few scattered rumors that Southwest and West Coast were dickering about a merger. Western had been discussing means for acquiring both Southwest and West Coast as a step in furtherance of the public interest, without warning of the pending merger. These discussions on Western's part sealed the reason, had a seal been necessary, for not attempting to file mutually exclusive applications in the two *Renewal Cases*.

On April 10, 1950 Southwest and West Coast filed an application with the Board for approval of a merger agreement between the two companies. This was the first



notice, other than bald rumors, received by Western that a merger between Southwest and West Coast was pending. Later it developed that negotiations were initiated as far back as July 14, 1949 and that some type of a written agreement concerning the merger was entered into as early as November 6, 1949. Concerning this most important subject, Member Harold A. Jones, in his affirmative statement on Western's petition for reconsideration of the order denying the consolidation, concurred in by Member Russell B. Adams (Appendix D), had this to say:

"United also called to the attention of the Board the conduct of counsel for Southwest at the same hearing, which conduct, to put it euphemistically, was evasive and misleading, and, from the record, an apparent effort to conceal that a merger agreement between Southwest and West Coast did in fact exist."

The application to merge the two companies created an entirely different climate to the two *Renewal Cases*, as effectiveness of the merger agreement was conditioned on both certificates being renewed for an additional five years. The moment the Merger Application was filed an *entirely new* route proceeding came into being. Where once there were two separate, unrelated applications—one to renew a 1200-mile temporary feeder route of one company terminating in the north at Medford, and the other to renew a 700-mile temporary feeder route of another company terminating at Medford on the south—there was now presented by the Merger Application, in effect and in fact, an application for a 2000-mile, single-company, regional system extending from Los Angeles to Seattle and beyond to Bellingham, totalling more than two-thirds of Western's route structure.

It was here for the first time that the real danger to Western's interests, and above and beyond all else to the public interest, came into sharp and direct focus. Overnight Western became threatened with a new, one-company, regional trunkline carrier that would be cloaked with great competitive advantages because of its 45 stations between Los Angeles and Seattle as against Western's 5. On May 2, 1950 Western's applications were filed.

On June 1, 1950 the Post Office Department presented a letter (Appendix B) to the Board recommending that favorable consideration be given to the granting of Western's petition to consolidate.

On June 6, 1950 the Board issued its order, Serial No. E-4292 (Appendix C), denying Western's petition to consolidate. This order was adopted by the votes of Chairman Joseph J. O'Connell, who resigned on July 10, 1950, and Members Josh Lee and Russell B. Adams, with Vice-Chairman Oswald Ryan and Member Harold A. Jones not present and not voting.

It is significant that the Board in this order recited that the two *Renewal Cases* and the *Merger Case* "are in certain respects interrelated to such an extent that it may prove advantageous and consistent with orderly procedure for the Board to decide the three cases simultaneously."

It is equally significant that the order recited "That in view of matters, such as the *new*<sup>2</sup> one-carrier, one-plane *service* that might be possible between points on the routes of Southwest and West Coast should the afore-

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<sup>2</sup>Emphasis in quoted material added throughout unless otherwise noted.

mentioned merger proposal be approved," *Southwest's Renewal Case* should be reopened and *West Coast's Renewal Case* reconvened for the purpose of receiving evidence with respect to the effect of the merger upon the suspension of some of United's points, adding that "any delay in the disposition of the renewal proceedings that may result from the action herein taken will not prejudice said carriers;"

The Board found that consolidation of the *Reopened Additional California-Nevada Service Case* would unduly expand the *scope* of the issues and that consolidation of Western's applications would unduly expand the issues (but not the scope) and "unduly delay the disposition thereof." It will be noted that the Board, by its language, conceded that Western's applications were *within the scope* of the issues created by the *Merger Case* to the extent and as that case revived and completely recolored the two *Renewal Cases*.

On June 26, 1950 Western filed with the Board a 31-page petition for reconsideration of the order denying consolidation. On June 26, 1950 this petition was denied for want of a majority, with two members, Oswald Ryan and Josh Lee opposing the petition and two members, Harold A. Jones and Russell B. Adams favoring it. A copy of the statement of Members Ryan and Lee opposing the consolidation, the statement of Members Jones and Adams favoring the consolidation and the order denying the petition for reconsideration for want of a majority are annexed to this brief as Appendix D.

It will be noted that in the negative statement of Members Ryan and Lee no consideration whatever is given to the public interest. On page 5 this statement is found:

“It [Western] further contends that the public interest requires consideration of the Pacific Coast air transportation problem as a whole and of possible savings to the Government that it claims would follow if its applications were granted. None of these arguments meets the objections resulting from Western’s long delay in filing its applications.”

And again on page 7:

“Whatever the merits of Western’s actions or non-action from its own point of view, it is nevertheless clear that *the carrier made a deliberate choice and must now abide by that choice.*”

And still again on page 8:

“The mere fact that Western may have been frustrated in its efforts to keep abreast of the merger negotiations between West Coast and Southwest does not mean that Western was thereby rendered powerless to protect its position. If Western feared the possibility of a merged feeder system on the West Coast, and wished to combat it by a proposal for rendering the service itself, Western could and should have filed timely applications to compete with the renewal applications of West Coast and Southwest.”

Thus, the two negative members charged Western with dereliction and default. Not a word of explanation is offered by the negative members as to why the *public interest* should be made to suffer by the dereliction of Western—be it ever so true.



Contrasted with this, the two affirmative members noted on page 3 of the affirmative statement:

“Under these circumstances the Board was called upon to make a determination whether to review these matters, together with the other matters discussed *infra*, in one proceeding in a *logical effort* to, with the broadest possible freedom, attempt to *determine the overall air transport needs of this very important area at one time*, with all the related facts and issues before it. The alternative was to ignore basic and important issues *directly affecting the welfare of the entire West Coast and the air transport system best fitted to serve this area*, and determine the issues on a case-by-case basis in what would amount to a succession of ‘keyhole’ approaches limited as to issues and scope of possible action.”

And on page 6:

“It seems *particularly indefensible* to refuse to hear the applications of Western for the operation of the West Coast feeder routes before deciding the applications of West Coast and Southwest for certificate renewal and approval of the merger proposal. *This amounts in practical effect to a refusal to hear issues which offer the prospect of saving the taxpayer at least \$750,000 annually, even though it would involve no disruption of present service or substantial prejudice to any carrier.* If the Southwest and West Coast certificates are renewed, and their proposed merger is approved, then *it is perfectly obvious that Western’s proposal will, as a practical matter, have been foreclosed.* In addition to the *important public interest elements involved*, such a procedure poses serious legal questions which should be carefully considered rather than disposed of in so cavalier a manner.”



Thus, the two negative members denied the consolidation because of *Western's* alleged default, whereas the *affirmative members would have approved it because the public interest would be benefited.*

It will be noted that Member Adams concurred in the original June 6, 1950 order of denial. Evidently he was convinced of his error by Member Jones. Had Chairman O'Connell not resigned prior to July 26 he too might have switched over with Mr. Adams, in which event this review would not have been necessary.

Thus a picture is presented under which, through circumstances of sheer chance, important rights of Western and compelling rights of the public will be trammelled and lost unless this Court intercedes to break the deadlock among four highly placed public officials. And this deadlock despite the fact that another important governmental agency which signs the checks, the Post Office Department, favors the consolidation.

### **C. Western Has Not Been Guilty of Laches and Is Not Chargeable With Dilatory Tactics.**

#### **(1) Western Acted With Promptness When Action Was in Order.**

It has been explained why Western did not file paralleling applications for consolidation with the *Southwest Renewal* and the *West Coast Renewal Cases* separately.

When the Merger Application was filed on April 10, 1950 Western moved with speed. Within less than three weeks Western held a meeting of its directors, who approved the program, organized Western Air Lines of the Pacific, Inc., as a new California corporation, prepared an application on behalf of Western Air Lines of the

Pacific, Inc. for a route from Los Angeles to Seattle and on to Bellingham, with the same stops that would be on the route of the Southwest-West Coast merged company, prepared an application to amend its own coastal route to conform precisely with the route that the merged company would have between Los Angeles and Seattle, prepared the technical application for permission to acquire stock ownership of Western Air Lines of the Pacific, Inc., and prepared the petition to consolidate these two mutually exclusive applications with the Southwest-West Coast Merger Application and the two Renewal Applications, both of which were tied to and, to all intents and purposes, became an integral and essential part of the Merger Application.

It may be pertinent here to speculate on why Southwest and West Coast lingered so long before filing the Merger Application. The two affirmative members of the Board, in their statement, said this:

“As stated before, West Coast and Southwest apparently sought to *conceal* the proposed merger from the Board *until after the prospective renewal cases had been decided*, and it was only brought to the Board’s attention as a result of a threat of subpoena.”

Renewal of Southwest’s 1200-mile experimental feeder system for an additional five years presented only innocuous prospects as far as it concerned Western’s rights and the public’s rights. The same innocent prospects were reflected by the projected extension of West Coast’s temporary feeder certificate. The fact that Western took only passive interest in these two proceedings, standing separately and alone, is ample and adequate evidence in support of this statement.

Western sprang into action the moment it was advised on April 10, 1950 by the Merger Application that action was in order. Western's promptness and Western's efforts to avoid dilatoriness are evidenced by this review. Western first learned on August 4, 1950 that its petition for reconsideration had been denied (although the Board had denied it for want of a majority on July 26, 1950). On the same day, it prepared the petition to review before this Court and obtained an order to show cause, copies of which were served on the Board in Washington the next day. In appraising Western's actions, comparison might be made of the actions of Southwest and West Coast in waiting until April 10, 1950 before filing their joint application for approval of the merger.

**(2) Western's Intentions With Respect to Future  
Procedural Steps.**

During the oral argument before this Court on August 14 Mr. Henry, when speaking for Southwest and West Coast, charged that Western was trying to "kill" the merger. This carried the connotation that Western's two route applications, its petition to consolidate and its petition for a review before this Court were merely steps in a delaying program.

If the Board will order a consolidation of the seven (or six, excluding the *Cal-Nevada Case*) cases, either under the mandate of this Court or by its own initiative, Western commits itself:

1. To prepare for the hearing on ten days' notice;
2. To present its direct affirmative case on its own applications in not to exceed two days (including cross-examination, over which Western would have no control);

3. To prepare and file its brief to the Examiner within seven days after completion of the consolidated hearing, and

4. To waive a brief to the Board and consent to oral argument as early as seven days after service of the Examiner's Report.

During the argument Mr. Goldman expressed the view that, if the proceedings were consolidated as requested by Western, the final decision would be two years away. If Southwest and West Coast will meet the time schedule to which Western will commit itself, the consolidated hearing could be concluded well before the end of this year.

By way of additional answer to Mr. Goldman's fear of a two-year delay, it should be noted that in a consolidated hearing there would be one brief, one Examiner's Report and one oral argument. This would take less time than would be required to conduct separate hearings, to prepare separate sets of briefs and to participate in separate oral argument before the Board in each of the several cases.

Should there be a delay of two years under a consolidated hearing, as predicted by counsel, it will have to be charged to the Board's lack of control over its own procedural mechanism and not to Western.



IV.

SUMMARY OF WESTERN'S POSITION  
AND ARGUMENT.

The basic factors behind Western's complaint against the Board's order denying consolidation is that the *public interest* was ignored. The fact that Western as a corporate entity may suffer irremedial damage in consequence of the Board's action is of minor importance to the public, however important it may be to Western.

By denying a consolidation with the *Merger Case* and the *Renewal Cases*, revised and recolored under light of the *Merger Case*, the public will be denied for five years in all events, and in all probabilities indefinitely, the great saving which Western can accomplish, aggregating in the neighborhood of three-quarters of a million dollars annually.

Even though inclusion of Western's applications along with the *Merger* and *Renewal Cases* might add a dozen or so days, or even a month or two, the rights of the public literally compel that a fair opportunity be given Western to prove that it can benefit the public by such a saving. It would be a travesty on justice and an indictment of our administrative processes if the public were denied the benefits that Western claims it can offer simply to save a few days or a few months.

An even greater denial of justice would result if the interests of the public and the rights of Western were foreclosed because of a two-to-two deadlock. Looking at this under light of the fact that the Post Office Department favors it, the very least that Western and the public are entitled to is a decision on the merits by this Court sitting as an arbiter over the four deadlocked members.

(1) The Public Interest Is Paramount.

Unquestionably, the selfish, "personal" rights of Western and of the would-be merged Southwest-West Coast company are at stake here. But those private interests, however important they may be to the respective corporate entities, must give way to the public interest.

While considering a matter involving the Civil Aeronautics Act, the Second Circuit Court, in *W. R. Grace and Co. v. C. A. B.*, 154 F. 2d 271 (1946), said: "With increasing emphasis the Supreme Court has admonished us that, in court review of such administrative orders as this now before us, *the public interest looms large*" and "The unmistakable fact is that, of recent years, there has been a steady development in Supreme Court decisions of the doctrine that those seeking review of the orders of administrative agencies, under review provisions like §1006 of this Act [Civil Aeronautics Act], 49 U. S. C. A. §646, *are primarily vindicating the public, not a private interest.*"

In similar vein, the Supreme Court in *Scripps-Howard Radio v. F. C. C.*, 316 U. S. 4, 86 L.ed 1229 (1942), said:

"The Communications Act of 1934 did not create new private rights. The purpose of the Act was to *protect the public interest* in communications. By §402(b)(2) Congress gave the right of appeal to persons 'aggrieved or whose interests are adversely affected' by Commission action. *But these private litigants have standing only as representatives of the public interest.*" (page 1236.)

Even if it were true that Western made a mistake in judgment in not filing a mutually exclusive application when the *Southwest Renewal Case* was initiated by the Board on April 4, 1949, assuming that Western could

have filed such an application which would have cut-off at Medford, and assuming that Western made a similar mistake in judgment after the *West Coast Renewal Case* was initiated by the Board on June 29, 1949, *the public interest must not be made to suffer by Western's mistake.*<sup>3</sup>

It is thus that Western appeals to this Court to consider the public interest, as the two affirmative Board members did and as the two negative Board members declined to do.

**(2) The True Effect of the Merger Application Was to Consolidate the Two Renewal Cases Into a Single New Renewal Case.**

Until the Merger Application was filed on April 10, 1950 Western had no warning and no notice that the two separate *Renewal Cases*—one involving 1216 miles with 25 stations and the other involving 688 miles with 21 stations, with a cut-off point at Medford—would emerge into a single, new route case involving 45 stations and almost 2000 route miles extending practically from border to border on the West Coast and paralleling with a single-carrier, single-plane operation the jugular vein of Western's system.

The Board's opinion and order to show cause in the *Southwest Renewal Case*, which started the proceeding, contain not the slightest hint that it might involve a new

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<sup>3</sup>That the public interest may require private parties to submit to delay is emphasized in *Landis v. North American Co.*, 299 U. S. 248, 81 L.ed. 153 (Dec. 7, 1936):

"We must be on our guard against depriving the processes of justice of their suppleness of adaptation to varying conditions. Especially in cases of extraordinary public moment, the individual may be required to submit to delay not immoderate in extent and not oppressive in its consequences if the public welfare or convenience will thereby be promoted." (page 159.)

border-to-border route. On the contrary, the Board stated:

"This certificate [Southwest's certificate for route 76] will expire on November 22, 1949, unless renewed by the Board. We have therefore made a careful review of the carrier's operating results, and on the basis of the information presently available to the Board, it is *our tentative conclusion* that a further experimental period of five years is warranted for *that* carrier." (page 10.)

This was tantamount to a notice to Western that the Board was going to renew Southwest's *existing* certificate for another five years unless convincing and compelling reasons to the contrary could be brought forward.

Had the Board's opinion and order to show cause in either *Renewal Case* presented the faintest inkling that "the Board's route program for re-examining the local feeder carrier experiment"<sup>4</sup> contemplated that consideration might be given to unifying Southwest's and West Coast's separate feeder routes into one border-to-border coastal route, or had Southwest and West Coast filed the Merger Application prior to commencement of the hearings on the *Renewal Cases*, as forthrightness compelled, there should be no doubt in any fair mind about the promptness with which Western would have acted. This assertion is proved irrefragably by the speed with which Western acted once the long delayed Merger Application was filed.

In a brittle effort to counteract the all-important and crucial effect of the *Merger Case* on the two separate

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<sup>4</sup>Page 13, Respondent's Memorandum in Support of Answer.



*Renewal Cases*, the two negative Board members who blocked the consolidation said in their statement:

“The possibility—or indeed the likelihood—of a proposal for merging the Southwest and West Coast systems has been obvious since the creation of these two carriers and those familiar with the airline industry have long been aware of the possibility of such a development.” (page 8.)

The basis of such a statement is clouded in mystery, particularly in face of the Board’s own decision creating Southwest and West Coast, in which this was announced:

“While the west coast area which is here involved is generally considered as an economic unit there are *two distinct trade areas involved*; namely, the Seattle-Portland area serving the northern part of the coast and the San Francisco-Los Angeles area serving the southern part. In establishing local feeder service it is our policy to authorize operations by local companies whose interests are centered in the area in which they will provide service. Establishment of a single local-feeder route extending from Los Angeles to Bellingham such as is here involved would result in the establishment of a line more than 1,000 miles in length serving both of the important trade areas. Although serving many intermediate points it would to a large extent parallel existing trunk-line services. *It appears from the record that insofar as local service is concerned there is a dividing line between the two areas at the Oregon-California boundary line.* North of Medford, which is close to that line, the principal traffic flows are into Seattle and Portland as the trade centers. South of Medford the flow of traffic is to San Francisco and Los Angeles. It is

significant that in presenting its case West Coast did not propose a connection between the northern and southern parts of its system, and during the course of the oral argument virtually abandoned its application for routes south of Oregon. Southwest was the only carrier suggesting the establishment of a continuous feeder system along the entire west coast area. *It is our conclusion, therefore, that two feeder systems should be set up to provide service over the routes which we have found required by the public convenience and necessity, one of which would extend north of Medford and the other south of that city. For any traffic which might develop between the areas connecting service will be possible at Medford either with the local carrier or with the trunk-line operator serving that city.*"<sup>5</sup>

This gave a fair indication, at least to Western, that there was not too much danger of these two relatively small and relatively harmless experimental feeder carriers being merged into a formidable, relatively large and relatively dangerous competitor. When the Board in the two orders to show cause initiating the two *Renewal Cases* gave no warning that such a situation was in prospect, and when the two carriers carefully shrouded in secrecy their negotiations for a merger while the hearings on the separate *Renewal Cases* were going on, Western naively continued to commit the "managerial mistake" of believing that there was no reason to take any affirmative action until April 10, 1950, when the truth came out.

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<sup>5</sup>*West Coast Case*, 6 C. A. B. 961, at page 996.

**(3) Consolidation Would Expedite Rather Than Delay  
Consummation of the Proceedings.**

It is perfectly obvious that the Board recognizes the need for tying the two *Renewal Cases* on to the *Merger Case* and completing the three in one decision or in concurrent decisions. The fact that the merger is conditioned on the two separate certificates being renewed alone is sufficient to weld the three together.

It is significant that after Western's petition to consolidate had been denied (but before its petition for reconsideration had been acted upon) the Board set the hearing on the *Merger Case* for August 7, 1950, the reopened hearing on the *Southwest Renewal Case* for August 14, 1950, the reconvened hearing on the *West Coast Renewal Case* for August 16, 1950 and the hearing on the *Reopened Additional California-Nevada Service Case* for August 18, if held in Washington, or August 21, 1950, if held in Los Angeles. This indicates that the four decisions will come down the stretch together.

If the two *Renewal Cases* and the *Merger Case*, either with or without the *Cal.-Nevada Case*, were consolidated with Western's two applications, a single decision on all of the cases almost certainly would come out ahead of separate decisions on the severally tried proceedings.

**(4) No Harm Would Result From Any Delay That  
Might Follow Consolidation.**

There has been and can be no showing that the public or any party would be harmed by the consolidation even though some delay would result. Under Section 9(b) of the Administrative Procedure Act the separate certificates of both Southwest and West Coast will continue effective until the Board finally acts—no matter how long the delay.

In the meantime, the traveling public will continue to receive the same service it has received for the past three and one-half years.

If anything, Southwest and West Coast could be benefited by any delay that might result from a consolidation. The assumption is that when the Board does reach a decision in the two *Renewal Cases* it will grant a certificate to each carrier (or the merged one carrier) for five additional years from the date of the decision. Thus, any interim delay will only add to the longevity of the life of the two carriers or the one merged carrier.

The charge that delays in merger cases might hamper voluntary route adjustments is equally untenable. There is not *one* case of a voluntary route adjustment, from merger, acquisition of assets or purchase of a route, which failed of completion because of procedural delays before the Board. Against this there are at least a few cases where the Board originally denied the voluntary agreement between the parties and the same parties later came back with revised agreements or proposals designed to meet the Board's objections.<sup>6</sup>

Against the lack of any real harm to either Southwest or West Coast or to the public if some delay were to attend a consolidation, there is imminent and positive danger of irremedial and permanent harm if the consolidation be denied.

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<sup>6</sup>*Marquette Case*, 3 C. A. B. 111 (1941); *Acquisition of Mayflower*, 4 C. A. B. 680 (June 12, 1944), 6 C. A. B. 139 (Aug. 7, 1944).



The Board, in its Memorandum in Support of its Answer, said with commendable frankness on page 18: "The Board agrees the applications here in question may be treated as mutually exclusive". During the oral argument Mr. Goldman, with equally commendable frankness, stated that if the Board approved the merger and renewed Southwest's and West Coast's certificates, from a practical standpoint, it would not grant either of Western's applications. With this acknowledgment, the subject need not be prolonged. It is worthy of note, however, that there is not a single instance of the Board having allowed competition among the feeders in any place in the United States. This conforms to the rigid policy established by the Board at the outset of the feeder experiment.

Thus, by the Board's own admission, if Western's two applications are not consolidated by the mandate of this Court, both of them will be denied even though a perfunctory "hearing" may be held. The Board will close the door against even listening effectively to Western's claim that it can operate a feeder service between Los Angeles and Seattle at least as good as that which the public has been receiving from Southwest and West Coast as separate carriers, and as good as that which a merged Southwest-West Coast carrier could perform, and at a saving to the taxpayers of \$750,000 annually. In five years this would amount to \$4,250,000. It is not overstating to say that the public interest literally demands that the Board hear Western's story before the door has been slammed shut.

In its Memorandum (page 11) and during the course of oral argument, the Board has noted that it might decide to deny renewal of the two certificates and that only if and when the Board should decide to renew the certificates and approve the merger will Western be harmed. Manifestly, this is true. But if the Board should come out with a decision renewing the certificates and should approve the merger, the harm will have been done. Thereafter, if this Court comes down with a mandate reversing the Board and ordering the cases to be consolidated, there will be nothing to consolidate. And this Court would not have the power to order the Board to unscramble its decisions and rehear them.

This situation creates an adequate picture of no possible harm flowing from a delay and of the real possibility of irreparable, irreparable and permanent harm if the consolidation be denied.

V.

THE ORDER HERE AT ISSUE IS  
REVIEWABLE.

The tenor of the briefs filed by the Board and the Interveners is to the effect that Western's petition for review is not meritorious. Although apparently not pressed, the suggestion also is made that the Board's order denying consolidation is procedural only, hence not final and not subject to review. The only treatment given to this point in the Board's brief is in the footnote on page 17, which reads in part: "In addition, there is considerable doubt that petitioner will ultimately prevail in this court because of a substantial question as to the court's jurisdiction to review the merits."

At this point a discussion of the legal right of review of the order as distinguished from its merits is timely. If the order be legally reviewable then the way is open for interlocutory relief upon a proper showing.

Section 285.11(a) of the Board's Rules of Practice provides:

"Any party may petition for rehearing, reargument, or reconsideration of any *final* order by the Board in a proceeding, or for further hearing before decision by the Board."

The Board accepted and acted upon Western's petition for reconsideration of the order denying consolidation. The petition for reconsideration was denied, not for want of jurisdiction because it was not a final order under Section 285.11(a) of the Rules of Practice, but only because the four members were equally divided.

There are only three court cases concerning the reviewability of an order of the Board denying a petition to con-

solidate. These three cases are controlling precedent that the order here is reviewable.

In *Pacific Overseas v. C. A. B.*, 161 F. 2d 633 (1946), the Board reopened the *Hawaiian Case* for reargument and reconsideration on the existing record. Shortly thereafter Pacific Overseas filed an application for a route from the mainland to Hawaii and petitioned to intervene in and have its application consolidated with the reopened proceeding. This the Board denied and a review was taken to the United States Court of Appeals for the District of Columbia. Without questioning its right to consider the order, the court granted a stay order and remanded the case to the Board.

The next case in order is *Eastern Airlines v. C. A. B.*, 178 F. 2d 726 (Nov. 30, 1949), likewise decided by the United States Court of Appeals for the District of Columbia. Eastern Airlines petitioned to have its application consolidated in the *New England States Case*, which the Board had limited to local or feeder service in the New England area. The court dismissed the petition on the grounds that Eastern's application was not within the scope of the *New England Case*, noting, however, "If petitioner had presented an application limited as the applications consolidated in the *New England Case* were limited the Board would have consolidated it for hearing with the others." Here Western's two applications square, point for point, with the merged Renewal Applications of Southwest and West Coast. Moreover, the Board has conceded that the applications involved in the consolidation order may be treated as mutually exclusive. Thus the *Eastern Airlines Case* is direct authority in support of the reviewability of the order here at issue.



The last case, by the same court, is *Seaboard & Western v. C. A. B.*, 181 F. 2d 777 (Dec. 5, 1949). In July, 1947 Seaboard & Western (no relation to Petitioner here) filed an application for a route between the United States and Europe. In December, 1948 Pan American and American Overseas Airlines filed a merger application. At that time there were three certificated American Flag carriers flying between the United States and Europe—Pan American, American Overseas (controlled by American Airlines) and T. W. A. All of the routes had some common points and each had some points not served by either of the others, but generally they were all competitive and they ran side by side rather than end-on as with Southwest and West Coast.

In March, 1949 Seaboard & Western petitioned the Board to consolidate its application with the merger case. This was denied and a petition for review followed. The petition was dismissed but only because the Board had given assurance that the North Atlantic route pattern would not be reconsidered. The court rightly held that in light of this the order denying consolidation was interlocutory and that, therefore, the court had no jurisdiction to review it. In the course of its decision, the court made these statements, which would seem to put an end to any question concerning Western's legal right to have the order here reviewed:

“Before entering upon consideration of the merits of the controversy, we are met with a contention of the Board that the court is without jurisdiction to review its order denying the consolidation. It says that order is merely procedural and interlocutory and that the jurisdiction of the court is limited to final orders. But ‘final’ in this connection does not mean

*a mere last in chronological sequence but means the effectual disposition of rights.*" (page 779.)

\* \* \* \* \*

"If the effect of the order denying consolidation in the case at bar were effectually to preclude Seaboard from rights which it otherwise would have, the order would be final as to Seaboard. It follows, as it frequently does in jurisdictional cases, for example, in the WJR case, that we must consider and decide a portion of the controversy on the merits in order to determine whether we do or do not have jurisdiction." (page 779.)

\* \* \* \* \*

"After the conclusion of an area case, carriers seeking certificates in the area have only such rights as are left open by the decision in that case. At the same time, it seems equally clear that if the Board has under consideration in a pending proceeding the fixing of routes, generally or of a specific nature, in an area and the selection of carriers to operate over those routes, *it must include in the proceeding* all pending applications for certificates over such proposed routes. Otherwise, the statutory right of excluded applicants to hearing and decision upon their applications would be futile." (pages 779-780.)

\* \* \* \* \*

"As we have said, it has no initial right to have the area case reopened; its right is to have its application considered in any proceeding in which general consideration of the area is reopened." (page 780.)

Significantly, in its order in the *Seaboard Case* (a copy of which is attached as an appendix to the Board's brief here), the court denied Seaboard's motion for a stay "without prejudice to its renewal when, as and if it appears

that the Board intends to invade Seaboard's right in the proceeding". This makes it plain that if the *Pan American-American Overseas Merger Case* had developed into a re-examination of the North Atlantic route or had it involved the merger of two non-competing, end-on routes, as we have here, a stay order would have issued.

Contrary to the case here, the facts in the *Seaboard Case* indicate that Seaboard's position would be bettered rather than worsened by the merger because it would reduce from three to two the number of American Flag carriers operating over the Atlantic and, to that extent increase Seaboard's chances of having its application granted when it came on for hearing in due course.

These cases, read under light of Section 1006 of the Civil Aeronautics Act, should dispel any doubt concerning the reviewability of the order here under scrutiny.

In passing, it is worthy of note that since the Board came into existence twelve years ago only four petitions to review orders denying consolidation have been filed, including the petition here. That strikes down any apprehension the Board might claim to have that its procedural mechanism will be derailed if the courts interfere in consolidation orders.

VI.

UNDER THE LAW THIS REVIEW IS  
MERITORIOUS.

Both in oral argument on August 14 and in its brief (page 18) the Board has conceded that Western's two applications are mutually exclusive with the two *Renewal Cases*.

On page 20 of its brief the Board denies that Western's applications are mutually exclusive with the Southwest-West Coast Merger Application. This takes too narrow a view of the subject. It is true that in the *Seaboard & Western Case*, to which reference has been made, the court held that the proposed merger of Pan American and American Overseas would not trespass on any rights of Seaboard, but that involved joining side-by-side routes with no renewal involved. But here we are concerned with the consolidation and renewal of end-on routes, which creates an entirely different picture. The Board recognized this large difference in the original denial order of June 6 when it found "that in view of matters such as the *new* one-carrier, one-plane *service* that might be possible between points on the routes of Southwest and West Coast should the aforementioned merger proposal be approved," the *Southwest Renewal Case* should be reopened and the *West Coast Renewal Case* reconvened. An expert mind is not required to know that no comparison exists between two separate and separately operated routes—one from Los Angeles to Medford, the other from Seattle to Medford—and a single through route, under a single operation, from Los Angeles to Seattle.



Apparently Southwest and West Coast recognize this, as the joint application for approval of the proposed merger contains this prayer:

“4. That an appropriate order be made and entered by the Board authorizing Southwest upon consummation of the proposed merger to engage in air transportation with respect to persons, property, and mail on all routes theretofore certificated to Southwest and West Coast;”.

However, after admitting, in effect, the applicability of the *Ashbacker Case*<sup>7</sup> by conceding that Western's applications are mutually exclusive with the two *Renewal Cases*, it is claimed that Western's applications were not filed in time. The inference is cast that a mutually exclusive application to come under the *Ashbacker Case* must be filed before commencement of the hearing on the first application.

The *Ashbacker Case* does not draw a line in administrative procedural processes on one side of which consolidation of mutually exclusive applications is mandatory and on the other side of which it is discretionary. In the *Ashbacker Case* itself, Fetzer filed the first application in March, 1944. In May, 1944 Ashbacker filed its application. On June 27, 1944 the Commission granted Fetzer's application without a hearing, as the Act permitted, and without first hearing Ashbacker's application, which was required under the Act before issuing a denial. Certainly the Fetzer application must have been processed well along to completion by the time Ashbacker's application was filed, as otherwise the granting order hardly could have been released in June.

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<sup>7</sup>*Ashlacker Radio Corp. v. F. C. C.*, 326 U. S. 327, 90 L. ed. 108 (Dec. 3, 1945).

In the *Seaboard & Western Case* the court said that, after the *conclusion* of an area case, carriers seeking certificates in the area have only such rights as are left open by the decision in that case and;

“At the same time, it seems equally clear that if the Board has *under consideration* in a pending proceeding the fixing of routes, generally or of a specific nature, in an area and the selection of carriers to operate over those routes, it *must* include in the proceeding all pending applications for certificates over such proposed routes.” (pages 779-780.)

A proceeding is *pending* until the Board's decision. The *Seaboard & Western Case* thus would lend more than faint color to an argument that the *Ashbacker Case* applies right up to the point of the Board's decision.

This hypothesis is not urged. Admittedly, a complete breakdown of an administrative agency's procedural activities could take place if a halt had to be called in a proceeding at *any* time a new mutually exclusive application were placed on file. In theory, to block out a would-be competitor, all an existing carrier would have to do would be to await the eve of the Board's decision, file a mutually exclusive application and cite the *Ashbacker Case*. That, of course, is an absurd extreme and the fact that it has not been done before this Board or any other board, at least so far as the reported cases go, is rather convincing evidence that there is little danger that it will be done.

Here we need not be troubled with the ordeal of attempting to fix a cut-off point. Western takes the position that under the circumstances involved in this particular case, and under the peculiar and special facts, either the Board committed a legal error or it abused its discretion.

It will be argued first that the *Ashbacker Case* is mandatorily applicable here, and second that an arbitrary abuse of discretion commands a reversal.

Indeed, it is doubtful that it would be proper for the courts to attempt to establish a formula designed to determine in any case when the *Ashbacker Case* would be mandatory and when only discretionary. In *F. C. C. v. Station WJR*, 337 U. S. 265, 93 L. ed. 1353 (1949), reversible error was claimed on the ground that the Commission had denied the right of oral argument. The court said this:

“It follows also that we should not undertake in this case to generalize more broadly than the particular circumstances require upon when and under what circumstances procedural due process may require oral argument. That is not a matter, under our decisions, for broadside generalization and indiscriminate application. It is rather one for case-to-case determination, through which alone account may be taken of differences in the particular interests affected, circumstances involved, and procedures prescribed by Congress for dealing with them. Only thus may the judgment of Congress, expressed pursuant to its power under the Constitution to devise both judicial and administrative procedures, be taken into account. Any other approach would be, in these respects, highly abstract, indeed largely in a vacuum.” (page 1361.)

**(1) The Facts Make Application of the Ashbacker Case Mandatory.**

Before treating with this point consideration should be given to the question of whether or not the *Ashbacker Case* requires a simultaneous hearing or simply a simultaneous decision. On page 24 of its brief the Board

claims that only a simultaneous decision is required even where the *Ashbacker Case* is mandatory. The *Ashbacker Case* itself does not decide the point, although there might be some dicta which could lead to a conclusion that separate hearings followed by simultaneous decisions would serve the purpose.

The Court of Appeals for the District of Columbia in *Kentucky Broadcasting Corp. v. F. C. C.*, 174 F. 2d 38 (1949), said:

“We hold that the Commission in this case accorded the parties hereto a full and fair *comparative hearing as required by the opinion of the Supreme Court* in *Ashbacker Radio Corp. v. Federal Communications Commission.*” (page 42.)

The same Court in *Radio Cincinnati v. F. C. C.*, 177 F. 2d 92 (1949), said at page 94: “Since the two applications were mutually exclusive, *this comparative hearing was required by the now-familiar doctrine of the Ashbacker case.*”

Whether mutually exclusive applicants are entitled to a comparative hearing or only comparative and simultaneous decisions need not be decided at this phase of the proceeding here. All will agree that the *Ashbacker Case* is mandatory up to the point of the commencement of the hearing. In effect and in fact, that point has not been reached in the seven cases sought to be consolidated. This is literally true of five of the seven—the *Merger Case*, the *Reopened Additional California-Nevada Service Case* and Western’s three applications.

The hearing before the Examiner in the *Southwest Renewal Case*, under its color before the *Merger Case* was filed on April 10, 1950, has gone through the hearing and past the Examiner’s Report. There yet remain



briefs to the Board, oral argument and the Board's decision. At this stage it would be very simple to reopen the record (as, in fact, the Board already has done) and consolidate that record into a single record in the consolidated proceeding. This would make it unnecessary to re-do that which already has been done and no time would be lost or wasted.

The *West Coast Renewal Case* has progressed to the point of substantial completion of the hearing. There yet remain receiving such additional evidence as might be pertinent for closing the hearing, briefs to the Examiner, the Examiner's Report, briefs to the Board, oral argument and the Board's decision. It would not even be necessary to reopen this case to include it among the consolidated cases as it has not been closed. What has been done would not have to be re-done. The transcripts of the hearing could be included with the transcript of the consolidated hearing.

Though it might be argued that *standing alone* both the *Southwest Renewal Case* and the *West Coast Renewal Case* have reached a procedural point where the *Ashbacker Case* would not apply to a newly filed, mutually exclusive application, it would be wrong to urge this argument under light of the effect of the *Merger Case*. It has been shown that the *Merger Case* completely and undeniably changed the two *Renewal Cases*. There is no escaping from the conclusion that when the *Merger Application* was filed on April 10, 1950, obviously under compulsion, the practical and only sensible effect of it was to establish a new, single, all-embracing proceeding, placing at issue (i) the extension not of two separate end-on routes but of one newly consolidated route extending from Los Angeles to Seattle and on to Belling-

ham, and (ii), provided the whole of that route were extended, the approval of the corporate unification of the two owners. *The hearing on that matter has not commenced.*

If the *Ashbacker Case* has any meaning, it must apply under these circumstances. Western urges that, under the unusual circumstances with which this review is cloaked, the *Ashbacker Case* is squarely and directly in point.

**(2) Even Though the Ashbacker Case Were Not Mandatory, a Reversible Abuse of Discretion Was Committed by the Two Negative Board Members.**

On page 18 of its brief the Board states, "The Board's action in refusing to consolidate petitioner's applications was clearly proper." Again on page 24, "Surely a procedural matter of this character is one for the Board to determine, unless there can be a clear showing of legal injury to one of the parties. And no semblance of such showing can be made here." Still again on page 26, "The reluctance of the Board to order a consolidated hearing of the cases in question is readily understood when it is realized how far some of the proceedings had already gone before petitioner sought consolidation." It is somewhat difficult to understand how the author of the brief was able to use such words as "clearly proper," "clear showing," "no semblance" and "reluctance of the Board" when *two* of the *four* members in strong language wanted to grant the consolidation.

The Act provides that Western is entitled to a hearing on its application (Section 40(c), 49 U. S. Code 481(c)). The cases hold that this hearing must be fair.

In *Ohio Bell Teleph. Co. v. Public Utilities Com.*, 301 U. S. 292, 81 L. ed. 1093 (Apr. 26, 1937), this was said:

“Regulatory commissions have been invested with broad powers within the sphere of duty assigned to them by law. Even in quasi-judicial proceedings there informed and expert judgment exacts and receives a proper deference from courts when it has been reached with due submission to constitutional restraints. [cases] Indeed, much that they do within the realm of administrative discretion is exempt from supervision if those restraints have been obeyed. *All the more insistent is the need, when power has been bestowed so freely, that the ‘inexorable safeguard’* [case] *of a fair and open hearing be maintained in its integrity.* [cases] *The right to such a hearing is one of ‘the rudiments of fair play’* [cases] assured to every litigant by the Fourteenth Amendment as a minimal requirement. [cases] *There can be no compromise on the footing of convenience of expediency, or because of a natural desire to be rid of harassing delay,* when that minimal requirement has been neglected or ignored.” (pages 1101-2.)

The courts reference to “a natural desire to be rid of harassing delay” should be given thoughtful attention. Claimed, but far from proved, delay which would result from the requested consolidation is the *only* argument advanced in justification of the acts of the two negative Board members who, by creating a deadlock, denied to Western the rudiments of fair play.

In *Interstate Commerce Commission v. Louisville & N. R. Co.*, 227 U. S. 88, 91, 57 L.ed. 431 (Jan. 20, 1913), the Supreme Court said “that administrative orders, quasi

judicial in character, are void if a hearing was denied; if that granted was inadequate *or manifestly unfair*;"<sup>8</sup>

Inasmuch as final denial of the petition to consolidate resulted from a deadlock among the four Board members, it might be argued that the error resulted from an unusual and unfortunate chance circumstance rather than from an abuse of discretion. But, in fact, the negative view of the two negative members amounts to an abuse of discretion and should be set aside by this Court. Any ruling which denies the rudiments of fair play to a hearing and rejects the spirit and intent of the statute involved is infected with an abuse of discretion.

In *Fox Film Corp. v. Trumbull*, 7 F. 2d 715 (Aug. 17, 1925), the District Court for Connecticut had this to say about discretion:

"The use of the words 'within the discretion of the commission' does not import absolute and capricious discretion. It is an administrative discretion, and it requires him to satisfy himself that such a state of facts exists that under the statute a reel is of 'strictly scientific character' or is 'for the promotion of educational, charitable, religious, and patriotic purposes and for the instruction of employees by employers of labor.' In deciding that question, he necessarily exercises discretion and judgment. It can be decided in no other way. *And in doing so he does not have unlimited license to act, irrespective of restraint. He must act in conformity with the intent and provisions of the statute.*" (page 727.)

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<sup>8</sup>Other cases containing equally forceful language are *St. Joseph Stock Yards Co. v. U. S.*, 298 U. S. 38, 80 L.ed. 1033 (Apr. 27, 1936); *Morgan v. U. S.*, 304 U. S. 1, 82 L.ed. 1129 (Apr. 25, 1938); *C. A. B. v. State Airlines*, 94 L.ed. 346 (Advanced Opinions, Feb. 6, 1950), and *Jones v. S. E. C.*, 298 U. S. 1, 80 L.ed. 1015 (Apr. 6, 1936).



In *Markall v. Bowles*, 59 F. Supp. 463, N. D. Cal., S. D. (Sept. 5, 1944), the Court said:

“So here the discretion vested in the Board must be exercised in the light of the *purposes of the statute* and the regulations promulgated pursuant thereto.” (page 465.)

\* \* \* \* \*

“When ‘discretion’ is abused, discretion becomes arbitrary. Decision then rests alone upon one’s will and not upon a process of reasoning nor upon considered judgment. *United States v. Lotempio*, D. C., 58 F. 2d 358, 360. Otherwise stated, it means acting according to one’s own will or pleasure, capriciously and without adequate determining principles.” (page 465.)

The spirit and intent of the Civil Aeronautics Act is found in Section 2, captioned “Declaration of Policy.”<sup>9</sup>

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<sup>9</sup>“Sec. 2 [49 U. S. Code 402]. In the exercise and performance of its powers and duties under this Act, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

“(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

“(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers;

“(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

“(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

“(e) The regulation of air commerce in such manner as to best promote its development and safety; and

“(f) The encouragement and development of civil aeronautics.”

"The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discrimination, undue preferences or advantages, or unfair or destructive competitive practices" will not be accomplished if two members of the Board have the discretionary power to deny not simply a *fair* hearing, but, in fact, *any* hearing, to an applicant that states it can save the Government \$750,000 a year.

Although the Civil Aeronautics Board may consist of experts in the field of civil aeronautics, no court should hesitate to issue proper directives when the circumstances warrant. Warrant most certainly is found when the injury comes not from the reasoned decision of a majority but only from a negative approach under a deadlock. And it must not be forgotten that the Post Office Department favored the consolidation.

"The ultimate test of reviewability is not to be found in an overrefined technique, but in *the need of the review to protect from the irreparable injury threatened in the exceptional case by administrative rulings* which attach legal consequences to action taken in advance of other hearings and adjudications that may follow, the results of which the regulations purport to control." *Columbia Broadcasting System v. U. S.*, 316 U. S. 407, 86 L.ed. 1563 (June 1, 1942) at page 1575.

"In the exercise of the judicial power to review questions of law, as conferred by an Act of Congress, *the seal of a United States Court should not become a mere rubber stamp for the approval of*

*arbitrary action by an administrative agency. Why, in the context, should any power of review whatever have been vested in the courts, unless Congress intended that such review should be judicially exercised?" General Tobacco & Grocery Co. v. Fleming, 125 F. 2d 596 (Feb. 5, 1942) at page 599.*

Even though a majority of the Board finally had ruled against consolidation, the facts in this case would have made it a clear and arbitrary abuse of discretion.

It is not too important whether the *Ashbacker Case* should have been applied mandatorily or discretionarily. Error was committed by the Board. This reveals adequate merit to Western's petition for review and requires that full consideration be given to the request for a stay order.

## VII.

### A STAY ORDER IS IMPERATIVE.

On page 10 of its brief the Board argues in effect that Western cannot be harmed unless and until the Board issues its decisions renewing the certificates of Southwest and West Coast and approving the merger, and that none of the administrative steps (presumably the hearings, briefs, Examiner's Report and oral argument to the Board) in any way could endanger Western. In addition, it is noted, but accepted in vain hope by Western, that the Board might in fact decide against the renewals or the merger.

The argument continues (page 11), "At that time [after the Board's decisions] the petitioner could request a stay, and if the Court were of the opinion that such relief was necessary, the Court could *then* stay the effectiveness of the Board's decision until judicial review of the Board's order denying consolidation had been completed." The fallacy of this argument is that once the Board has reached its decisions there would be nothing to consolidate with Western's applications. Even though armed with a mandate of this Court, Western at that time would be in the position of having a right without a remedy.<sup>10</sup> The mandate of this Court directing the Board to consolidate the four pending proceedings (which then would not be pending) with Western's three pending proceedings would

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<sup>10</sup>A somewhat comparable situation is found in *Bardwell v. Turner*, 219 Cal. 228 (Oct. 20, 1933). Defendants appealed to the California Supreme Court from an order of the Superior Court denying their motion for a change of venue from Kern County to Los Angeles County and applied for a writ of *supersedeas* pending the appeal, which was granted by the Supreme Court. Defendants could have been harmed only if the lower court went to trial in Kern County, decided against defendants, and the Supreme Court thereafter reversed the order denying the change of venue.



be meaningless. That mandate could not serve to reverse the Board's decisions or serve to compel the Board to reopen those decisions.

Western as an intervener in those cases could petition the court for a review of the decisions. However, lacking a comparative record or comparative decisions from which the reviewing court could determine whether the Board had erred in granting the combined Southwest-West Coast applications against Western's application, the court review of the decisions would be empty.

Issuance of a stay order against an administrative agency pending a review of its order is by no means unusual.

"No court can make time stand still. The circumstances surrounding a controversy may change irrevocably during the pendency of an appeal, despite anything a court can do. *But within these limits it is reasonable that an appellate court should be able to prevent irreparable injury to the parties or to the public resulting from the premature enforcement of a determination which may later be found to have been wrong.* It has always been held, therefore, that, as part of its traditional equipment for the administration of justice, a federal court can stay the enforcement of a judgment pending the outcome of an appeal. [cases] (page 1234.)

\* \* \* \* \*

"If the administrative agency has committed errors of law for the correction of which the legislature has provided appropriate resort to the courts, such judicial review would be an idle ceremony if the situation were irreparably changed before the correction could be made." (page 1234.)

*Scripps-Howard Radio v. F. C. C.*, 316 U. S. 4, 86 L.ed. 1229 (Apr. 6, 1942).

*Merchants Warehouse Co. v. U. S.*, 283 U. S. 501, 75 L.ed. 1227 (May 18, 1931), involving an order of the Interstate Commerce Commission canceling certain tariffs in which a stay order was issued, presents an interesting slant to the case here since the court noted that the legality of the matter in dispute was not free from doubt, as the judges of the court below were not unanimous:

*"The court below was within the limits of its discretionary power in staying the Commission's order pending the appeal. The practice complained of was of long standing, entered into, so far as appears, in good faith, at a time when the discrimination, if it existed, was much less serious than at present, and before the present prohibitions against such discriminations. Its legality now is not free from doubt, as is indicated by the fact that the judges of the court below were not UNANIMOUS. The immediate enforcement of the order if the judgment below were not affirmed here would have resulted in a serious and unnecessary disturbance of a course of business affecting not alone the parties to this litigation, but the patrons of the various warehouses, which the court below found would be irreparable. These considerations, taken together, were sufficient to call for the exercise of its discretion."* (pages 1238-9.)

If lack of a unanimous decision is a factor justifying a stay order pending a review, a *deadlocked* "decision" should be close to a compelling reason for issuing a stay order.

Although under a different statute, and thus not directly in point, the case of *Lambros v. Young*, 145 F. 2d 341 (Oct. 30, 1944), decided by the Court of Appeals, Dis-

trict of Columbia, is pertinent as it involved a deadlocked, one-to-one decision of the Commissioners of the District of Columbia on appeal from a ruling of the Alcoholic Beverage Control Board revoking a liquor license:

“Even if the judicial rule [affirmance of lower court when appellate court evenly divided] could be applied by analogy we should be slow to read rigid judicial precedents into an administrative statute. One of the purposes of administrative law is to permit a more elastic and informal procedure than is possible before our more formal courts. The result for which the Commissioners argue here is inelastic and seems to us *unfair*. *It deprives appellants of their license in a case where the Commissioners have been unable to reach a conclusion* whether they are guilty or innocent of the criminal charges which justify revocation of their right to carry on their business.” (page 343.)

\* \* \* \* \*

“It follows that an injunction should issue against the enforcement of the order revoking appellants’ license which will terminate when the appeal is reinstated.” (page 343.)

The complete lack of any danger of real harm to the public or to Southwest or to West Coast from the effects of a stay order, and the real possibility that Western’s right to a fair hearing on its applications may be completely and forever lost in the absence of a stay order present circumstances compellingly in favor of a stay order pending the review on its merits. This will give assurance that the processes of this Court will not be futile and that an irretrievable injustice will not be committed.

## CONCLUSION.

Denial of consolidation of Western's applications with the *Southwest-West Coast Cases* was equivalent to denying a fair hearing to Western. This is intolerable to the law.

Failure to enjoin the Board from going forward to conclusion with the *Southwest-West Coast Cases* could put to naught the mandate of this Court if the Board were reversed on the merits of the review. The right to an effective Court review and enjoyment of the fruits of a favorable Court decision should not be under indirect but effective control of the administrative agency whose order is under review.

An appropriate stay order should be issued by this Court.

Respectfully submitted,

HUGH W. DARLING,

GEORGE G. GUTE,

*Attorneys for Petitioner.*

GUTHRIE, DARLING & SHATTUCK,

*Of Counsel.*

August 19, 1950.



**Certificate of Service.**

I certify that on this date I will have caused to be served by mail, properly addressed, with postage prepaid, copies of the foregoing Brief upon the attorneys of record for Respondent and for Interveners.

Los Angeles, California, August 19, 1950.

GEORGE G. GUTE,  
*Attorney for Western Air Lines, Inc.*





## APPENDIX A.

Before the Civil Aeronautics Board.

In the Matter of the Petition of Western Air Lines, Inc. Under Title X of the Civil Aeronautics Act of 1938, as Amended, and Part 285 of the Rules of Practice for an order of consolidation.

### PETITION OF WESTERN AIR LINES, INC., FOR AN ORDER OF CONSOLIDATION.

Western Air Lines, Inc. respectfully petitions for an order of this Board consolidating in one proceeding for hearing and disposition the following proceedings:

1. Docket No. 3718—Concerning the renewal of the certificate for Route 76 held by Southwest Airways Company and the suspension in part of the certificate for Route 1 held by United Air Lines, Inc.
2. Docket No. 3966—Concerning the renewal of the certificate for Route 77 held by West Coast Airlines, Inc. and the suspension in part of certificates for Routes 1 and 57 held by United Air Lines, Inc.
3. Docket No. 4405—Concerning the proposed merger of West Coast Airlines, Inc. into Southwest Airways Company.
4. Docket No. 2019 *et al.*—Concerning the matters, applications and orders to show cause pending for hearing and determination in the Additional California-Nevada Service Case.
5. Docket No. 4447—Concerning the application of Western Air Lines, Inc. for additional intermediate points in the states of California, Oregon and Washington on its Route 63.



6. Docket No. 4448—Concerning the application of Western Air Lines of the Pacific, Inc. for a certificate of public convenience and necessity for a route between Los Angeles, California and Bellingham, Washington by way of various intermediate points.
7. Docket No. 4449—Concerning the application of Western Air Lines, Inc. for approval of the acquisition of complete stock ownership of Western Air Lines of the Pacific, Inc.
8. Any other matters, applications, petitions and orders to show cause pending before the Board which might be affected by or have effect on any of the foregoing matters.

Points and Authorities Relied Upon  
in Support of This Petition.

I.

Title X of the Act and Part 285 of the Economic Regulations, coupled with recognized precedent, give the Board ample power to consolidate separate and several matters pending before the Board into one proceeding when that course of action appears to be in the public interest and beneficial to the rights of the various parties concerned.

II.

The seven separate proceedings sought to be consolidated in one proceeding are all interrelated. The Board's decision in each will have some pressure on each of the other proceedings.

The interrelationship of Item 1 (the renewal of Southwest's certificate for Route 76), Item 2 (the renewal of

West Coast's certificate for Route 77) and Item 3 (the merger of West Coast into Southwest) is adequately self-evident.

The relationship of Item 4 (concerning the revived portion of the original California-Nevada Service Case) to Items 1, 2 and 3 is equally self-evident. If the Board should refuse to extend Southwest's certificate under Item 1, and thus allow it to expire *sine die*, there would be little use in granting Southwest's applications which have been consolidated into Item 4.

Item 5 (concerning Western's application for additional points on Route 63) and Item 6 (concerning the application of Western Air Lines of the Pacific) were framed especially and specifically for the purpose of enabling the Board to determine on competent evidence whether the public interest might be served better and more economically if a feeder service in the Pacific Coast area where operated either by an established regional trunkline carrier directly or by an established regional trunkline carrier through a wholly-owned subsidiary. If consolidated into one proceeding, the Board will have in front of it, side by side, all evidence, including the cost, relating to the operation of a feeder service in the Pacific Coast area (a) by Southwest and West Coast separately, (b) by Southwest alone under the proposed merger of West Coast, (c) by Western under its own operation and (d) by Western through a wholly-owned subsidiary. The value to the Board, to the taxpayers and to the applicants of the advantages of having such a complete picture in one frame is inestimable.

Item 7 (concerning the acquisition by Western of control of Western Air Lines of the Pacific) necessarily is

welded to Item 6, which in turn is linked to Item 5, which in turn, as has been shown, bears upon Item 4, 3, 2 and 1.

Item 8 (concerning all other matters) has been included in the event other applications, which would be subject material for consolidation, should be filed subsequent to the order of consolidation under this petition and prior to the consolidate hearing.

### III.

By combining the seven interrelated proceedings into one proceeding for a single hearing and a single decision, a complete and comprehensive record will be made enabling the Board to place each application in clear focus with each of the other applications. This will tend to give assurance that the over-all public interest will not be submerged in favor of the interests of only one class of the public or in favor of the interests of only a portion of the area involved. In addition, substantial savings in time and effort indubitably will accrue, as a good deal of evidence pertinent to one application would be equally pertinent to many, if not all, of the others, thus avoiding the re-introduction of similar evidence in successive cases separately heard. The time required to hear, brief, argue and decide all of the proceedings in one consolidated proceeding will be considerably less than the time that would be consumed in hearing, briefing, arguing and deciding each case separately. This will redound to the public interest and will foster orderly and expeditious proceedings before the Board.

IV.

Consolidation into one proceeding of the interrelated proceedings will sprout benefits in the form of assurance that the over-all public interest will be kept in proper perspective and in the form of expedition and saving of time and labor, as well as saving in procedural cost. These benefits commend this petition to favorable action by the Board.

In the absence of a clear showing of consequent injury of significance to an interested party, an order of consolidation should be made.

Respectfully submitted,

WESTERN AIR LINES, INC.

By /s/ Terrell C. Drinkwater  
Terrell C. Drinkwater  
President



VERIFICATION.

State of California, County of Los Angeles—ss:

Terrell C. Drinkwater, being first duly sworn, deposes and says that he is President of Western Air Lines, Inc., the Petitioner in the foregoing document; that he has read and is familiar with the contents thereof; that he intends and desires that in granting or denying the relief requested the Board shall place full and complete reliance upon the accuracy of each and every statement therein contained; that he is familiar with the facts therein set forth and that to the best of his information and belief every statement contained in the foregoing document is true and no such statement is misleading.

/s/ Terrell C. Drinkwater  
Terrell C. Drinkwater  
President

Subscribed and sworn to before me this 27th day of April, 1950.

/s/ Earnest H. Brown  
Notary Public in and for the County of Los Angeles,  
State of California

My Commission expires December 5, 1952.

CERTIFICATE OF SERVICE.

I certify that on this date I will have caused to be served by mail, properly addressed, with postage prepaid, copies of the foregoing Petition upon the attorneys of record for all parties who may be concerned.

Dated: May 2, 1950, Los Angeles, California

/s/ D. P. Renda  
D. P. Renda  
Assistant Secretary and Attorney





APPENDIX B.

Address Reply To  
"THE SOLICITOR"  
And Refer To  
Initials and Number  
JTC:eb

POST OFFICE DEPARTMENT  
Office of the Solicitor  
Washington 25, D. C.

June 1, 1950

Civil Aeronautics Board  
Department of Commerce Building  
Washington 25, D. C.

Re: Docket No. 3019, et al: Reopened portions of  
the California-Nevada Service Case.

Docket No. 3718: Southwest Extension/United  
Suspension Case.

Docket No. 3966: West Coast Extension/  
United Suspension Case.

Docket No. 4405: Southwest/West Coast  
Merger Case.

Docket No. 4447: Application of Western Air  
Lines for additional intermediate points on  
Route No. 63.

Docket No. 4448: Application of Western Air  
Lines of the Pacific for a certificate of public  
convenience and necessity.

Docket No. 4449: Application of Western Air  
Lines for approval of acquisition of control of  
Western Air Lines of the Pacific.



Gentlemen:

Western Air Lines has filed a Motion for an Order of Consolidation of all of the above-described dockets into one proceeding, and in further support there has been filed a Supplemental Memorandum alleging that combining the operations of Southwest Airways and West Coast Airlines with those of Western Air Lines would result in a potential savings to the Government of approximately \$750,000, annually. The Post Office Department is a party in the first three cases listed.

The Department urges that there be a complete rather than a piecemeal examination of the matters involved, and a full examination into potential savings before final decision on renewal of the temporary certificates in issue. It is therefore respectfully recommended that favorable consideration be given to granting of the aforesaid Motion.

Very truly yours,

(Signed) Frank J. Delany

Frank J. Delany

Solicitor

cc: All parties,

Dockets Nos. 3019, 3718, 3966,  
4405, 4447, 4448, and 4449.





## APPENDIX C.

Orders Serial Number E-4292.

United States of America, Civil Aeronautics Board,  
Washington, D. C.

Adopted by the Civil Aeronautics Board at its office in  
Washington, D. C., on the 6th day of June, 1950.

In the matter of the

Southwest-West Coast Merger Application,  
Southwest Renewal-United Suspension Case,  
West Coast Renewal-United Suspension Case,  
Reopened Additional California-Nevada Service Case,  
Western Air Lines, Inc.

Application for additional intermediate points in the  
states of California, Oregon and Washington on its  
Route 63,

Western Air Lines of the Pacific, Inc.

Application for a certificate of public convenience and  
necessity for a route between Los Angeles, California  
and Bellingham, Washington by way of various in-  
termediate points, and

Western Air Lines, Inc.

Application for approval of the acquisition of com-  
plete stock ownership of Western Air Lines of the  
Pacific, Inc.

Docket Nos. 4405, 3718 *et al.*, 3966 *et al.*, 2019 *et al.*,  
4447, 4448, 4449.

### ORDER.

United Air Lines, Inc. (United), having filed a motion  
with the Board on April 27, 1950, requesting, *inter alia*,  
(a) severance from the *Southwest Renewal-United Sus-*



*pension Case*, Docket No. 3718 *et al.*, and the *West Coast Renewal-United Suspension Case*, Docket No. 3966 *et al.*, of the issues of renewal of the certificates of public convenience and necessity of Southwest Airways Company (Southwest), and West Coast Airlines, Inc. (West Coast), (b) consolidation of the severed portions of the certificate renewal proceedings with the *Southwest-West Coast Merger Case*, Docket No. 4405, for hearing and decision, (c) deferment of all further procedural steps with respect to the remainder of the aforementioned *Southwest Renewal-United Suspension Case* and *West Coast Renewal-United Suspension Case* and deferment of the *Reopened Additional California-Nevada Service Case*, Docket No. 2019, *et al.*, until after final decision upon the proposed merger and, in the event of approval thereof, until after operating experience has been obtained under the merger;

United having represented in support of its motion, *inter alia*, that the issues of the certificate renewal cases and the merger application are closely interwoven and can be disposed of together expeditiously; that the factual situation underlying the suspension-substitution aspects of the *Southwest Renewal-United Suspension*, *West Coast Renewal-United Suspension* and the *Reopened Additional California-Nevada Service* cases has changed as result of the proposed merger of Southwest and West Coast; that such factual changes, in the event of approval of the proposed merger will seriously affect the validity of various findings and conclusions set forth in the Examiner's Report in the *Southwest Renewal-United Suspension Case*;

that essential facts will not be available to consider the aforesaid issues of suspension and substitution contemporaneously with the issues of the *Southwest-West Coast Merger Case*; that consolidation of the aforementioned suspension-substitution issues into the *Southwest-West Coast Merger Case*, would materially enlarge the scope of that case and prevent expeditious disposition of the merger application; that United's various proposals will result in a more orderly disposition of the issues of the aforementioned proceedings;

Western Air Lines, Inc. (Western), having filed with the Board on May 2, 1950, an application, Docket No. 4447, requesting amendment of its certificate of public convenience and necessity for route No. 63 so as to extend said route beyond Seattle-Tacoma, Wash., to the terminal point Bellingham, Wash., and add certain intermediate points between Los Angeles, Calif., and Bellingham, Wash.;

Western Air Lines of the Pacific, Inc. (Pacific), having filed with the Board on May 2, 1950, an application, Docket No. 4448, requesting a certificate of public convenience and necessity authorizing it to engage in air transportation between Los Angeles, Calif., and Bellingham, Wash., via various intermediate points;

Western having filed with the Board on May 2, 1950, Docket No. 4449, an application, *inter alia*, under section 408 of the Act, requesting approval of the acquisition by Western of the controlling stock interest of Pacific;

Western having filed with the Board on May 2, 1950, a petition requesting, *inter alia*, that the Board consolidate the aforementioned applications of Western and Pacific with the aforementioned proceedings in Docket Nos. 3718, 3966, 4405, and 2019 *et el.*;

Western having represented in support of its petition, *inter alia*, that the proceedings, Docket Nos. 3718, 3966, 4405, and 2019 *et al.*, are all interrelated; that Western's application, Docket No. 4447, and Pacific's application, Docket No. 4448, were framed to enable the Board to determine whether the public interest might be better and more economically served if a feeder service in the Pacific coast area were operated either directly by a regional trunkline carrier or by a wholly owned subsidiary thereof; that consolidation of all of the aforementioned proceedings will make available to the Board all essential evidence including the cost of operating feeder service in the Pacific coast area (a) by Southwest and West Coast separately, (b) by Southwest alone, under the proposed merger of Southwest and West Coast, (c) by Western, and (d) by Western through a wholly-owned subsidiary, Pacific; that Western's application for approval of its acquisition of Pacific, Docket No. 4449, is directly related to the aforementioned applications of Western and Pacific, under section 401 of the Act; that consolidation of the aforementioned seven interrelated proceedings into one proceeding for a single hearing and decision will provide the Board with a complete and comprehensive record relating to the over-all public interest; that substantial savings in

time and effort with respect to disposition of said proceedings will result from consolidation thereof;

Southwest and West Coast having filed with the Board on May 10, 1950, a joint motion in opposition to the aforesaid motion of United and petition of Western requesting, *inter alia*, that the Board deny United's motion and Western's petition; that the record be closed in the *West Coast Renewal-United Suspension Case*; that the Board defer the suspension and substitution issues in both of the aforementioned renewal-suspension proceedings for decision with the *Southwest-West Coast Merger Case*; that said merger case be broadened to embrace an issue with respect to the effect of merger approval upon the various suspension and substitution issues; and that the merger case and the aforementioned suspension substitution issues be decided concurrently;

Western having filed with the Board a memorandum and supplemental memorandum in support of its petition herein; and the Post Office Department having filed with the Board a letter in support of said petition;

Southwest having filed with the Board a letter in opposition to Western's aforesaid supplemental memorandum;

The Board, upon consideration of the aforementioned applications, motions, petitions, and memoranda, finding:

1. That although the aforementioned *Southwest Renewal-United Suspension Case*, Docket No. 3718 *et al.*, the *West Coast Renewal-United Suspension Case*, Docket No. 3966 *et al.*, and the *Southwest-West Coast Merger*



*Case*, Docket No. 4405, are in certain respects inter-related to such an extent that it may prove advantageous and consistent with orderly procedure for the Board to decide the three cases simultaneously, United has not established that (a) severance of the renewal issues from Docket Nos. 3718 *et al.*, and 3966 *et al.*, and consolidation of such issues with Docket No. 4405; or (b) deferral of all further procedural steps in Docket No. 2019 *et al.*, and on the suspension-substitution issues in Docket Nos. 3718 *et al.*, and 3966 *et al.*, is required as a matter of law or that the benefits that might flow from such action, when weighed against the undesirable results that would stem therefrom, warrant such action as a matter of Board discretion;

2. That in view of matters such as the new one-carrier, one-plane service that might be possible between points on the routes of Southwest and West Coast should the aforementioned merger proposal be approved, the *Southwest Renewal-United Suspension Case*, Docket No. 3718 *et al.*, should be reopened, and the *West Coast Renewal-United Suspension Case*, Docket No. 3966 *et al.*, should be reconvened for further hearing in order that evidence may be adduced with respect to the effect, if any, of the aforementioned merger proposal upon the substitution-suspension issues in said proceedings; that since Southwest and West Coast will continue, until final disposition of their certificate renewal applications in Docket Nos. 3718 *et al.*, and 3966 *et al.*, to hold operating authority over their respective routes by virtue of the provisions of section

9(b) of the Administrative Procedure Act, any delay in the disposition of the renewal proceedings that may result from the action herein taken will not prejudice said carriers;

3. That consolidation of the *Reopened Additional California-Nevada Service Case*, Docket No. 2019 *et al.*, with Docket Nos. 3718 *et al.*, 3966 *et al.*, or 4405, would unduly expand the scope of the issues in each of said proceedings and unduly delay the disposition thereof; that deferral of said proceeding would unduly delay the disposition thereof;

4. That consolidation of Docket Nos. 4447, 4448, and 4449 with Docket Nos. 3718 *et al.*, and 3966 *et al.*, or Docket No. 4405 would unduly expand the issues in such proceedings, unduly delay the disposition thereof, and is not conducive to the proper dispatch of the Board's business;

5. That, with respect to all other relief sought, the various motions, petitions, and memoranda herein fail to set forth facts which would warrant the granting of such relief;

It Is Ordered:

1. That the *Southwest Renewal-United Suspension Case*, Docket No. 3718 *et al.*, be and hereby is reopened and the *West Coast Renewal-United Suspension Case*, Docket No. 3966 *et al.*, be and hereby is reconvened for further hearing for the purpose of permitting additional evidence to be adduced solely on the question of the effect,

if any, upon the substitution-suspension issues in said proceedings of the proposed merger of Southwest and West Coast;

2. That the aforesaid motions and petitions, except to the extent granted herein, be and hereby are denied.

By the Civil Aeronautics Board:

/s/ M. C. Mulligan  
M. C. Mulligan  
Secretary

(Seal)







APPENDIX D.

E-4484

UNITED STATES OF AMERICA  
CIVIL AERONAUTICS BOARD  
WASHINGTON, D. C.

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Served: August 4, 1950

DOCKETS NOS. 4405, ET AL.  
SOUTHWEST-WEST COAST  
MERGER APPLICATION, ET AL.

Decided: July 26, 1950

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Petitions of Western Air Lines, Inc. and United Air Lines, Inc. for reconsideration of Order Serial No. E-4292, dated June 6, 1950, denied.

Statment of Ryan, Acting Chairman, and Lee,  
Member, in support of denial of petitions.

This opinion involves our consideration of petitions by Western Air Lines, Inc. (Western), and United Air Lines, Inc. (United), for reconsideration of Order Serial No. E-4292, dated June 6, 1950. That order, which was adopted unanimously by the Board members who participated in such action, denied various requests made by Western and United with respect to procedure in the handling of seven proceedings relating to air service in the Pacific Coast area. The Board members participating in reconsideration have divided evenly on the action to be taken on the petitions for reconsideration, and the petitions have therefore failed for lack of a majority.

The original petition of Western requested consolidation for purposes of hearing and decision of these seven proceedings involving the renewal of temporary certificates of Southwest Airways

[2]

Company (Southwest) and West Coast Airlines, Inc. (West Coast), the proposed suspension of various points on the routes of United, Western and Frontier, the proposed merger of Southwest and West Coast, the application of Southwest and Bonanza for routes from Los Angeles to Phoenix, and applications of Western for authorization to provide services either in its own right or through a subsidiary (Western of Pacific) over the routes now served by Southwest and West Coast. The applications of Western and Western of Pacific were not filed until after hearing and issuance of the examiner's report in the Southwest Renewal-United Suspension Case and substantial completion of the hearing in the West Coast Renewal-United Suspension Case. Order Serial No. E-4292 reopened or reconvened hearing in both cases to take evidence only as to the effect of the proposed Southwest-West Coast merger upon the issues relating to suspension of United points.

In its original petition and supporting memoranda, Western principally argued that the proposed merger of Southwest and West Coast would create excessive competition for Western and United, that it could operate the Southwest-West Coast feeder routes at an annual saving to the Government of a substantial sum, and that the

Board should consider problems of air service on the Pacific Coast as a whole and not in several proceedings. In Order Serial No. E-4292, the Board found that the consolidation

[3]

of the applications of Western and Western of Pacific would unduly expand the scope of the issues in each of the other proceedings involved, would unduly delay the disposition thereof, and would not be conducive to the proper dispatch of the Board's business. Accordingly, the Board denied the petition.

In its petition for reconsideration of the Board's order and its reply to answers of West Coast and Southwest in opposition thereto, Western has reiterated the arguments of its original petition which we previously found insufficient to warrant the delay and disruption of existing proceedings which would result therefrom. In addition, Western has urged certain contentions not found in its original petition. In our judgment, however, Western has not now advanced any facts or contentions which warrant a change in the findings in said order, and hence the petition for reconsideration should be denied.

One of the major difficulties confronting Western in its request for consolidation is the fact that its own applications for authorization to serve the feeder routes now being operated by Southwest and West Coast were filed long after the proceedings on the renewal of the certificates of West Coast and Southwest for those routes and the suspension of various points in the areas now served by

United had been instituted and only after such proceedings reached the advanced procedural stages indicated above. This fact not only eliminated any legal grounds that Western might urge in support of consolidation of its application with those proceedings, but it also substantially diminished the weight of its arguments to the effect that the public interest requires consolidation.

[4]

In its petition for reconsideration, Western argued that the Board is required to grant the requested consolidation by the holding in *Ashbacker Radio v. Federal Communications Commission*, 326 U. S. 327 (1945). Consolidation is required only where refusal thereof would deny the applicant that hearing upon its application to which it is entitled under all the circumstances. No such right is being denied Western. It is clear that the principles of the *Ashbacker* case do not require consolidation of a route application with other route proceedings in which public hearings have been substantially completed, even though they are alleged to be mutually exclusive. Nor do the principles of this case require the consolidation of an application for routes and an application for approval of a merger, since these are not mutually exclusive, and inclusion of the route proceedings in the merger case would greatly enlarge the issues in that proceeding.

Western also argues that its applications involve the same type of service as is proposed by Southwest and West Coast and, therefore, fall within the language of the court in *Eastern Air Lines, Inc. v. Civil Aeronautics Board*



(78 F. 2d, 726, 1949). Here again it is clear that the *Eastern* case is not applicable where one of the applications concerned has not been seasonably filed.

Western further contends that considerations of public interest require the Board to grant consolidation in this instance. In support of this contention, Western cites findings in our previous

[5]

order as to the relationship between the renewal-suspension cases and the merger proceeding, the reopening of the renewal-suspension cases and receipt of evidence as to the effect, if any, of the merger upon the “suspension-substitution” issues in said proceedings, and that neither Southwest nor West Coast would be prejudiced by the delay that might be involved in such action.

It further contends that the public interest requires consideration of the Pacific Coast air transportation problem as a whole and of possible savings to the Government that it claims would follow if its applications were granted. None of these arguments meets the objections resulting from Western’s long delay in filing its applications. Nor do they take account of the difference between the effect of the limited reopenings made by the Board in its prior order and of the sweeping scope of the proceeding which would result from the consolidations requested by Western. Although we did find in the prior order that there was a sufficient relationship between the renewal-suspension cases and the merger case to warrant reopening the former cases for a limited purpose, and that the delay caused by this

action was not prejudicial to Southwest or West Coast, such findings do not fit a situation in which we are requested to consolidate seven proceedings, all of which involve issues of a substantial nature and which can only create an unwieldy case and prolonged delays. Hence, after considering the matters of public interest

[6]

asserted by Western, we find that they are outweighed by the public interest in orderly conduct of the Board's business and in avoiding undue delay in disposition of the issues in the other proceedings. Furthermore, as an intervener, Western will have a full opportunity in the merger proceeding to introduce any relevant evidence on public interest aspects of the Southwest-West Coast merger proposal, including evidence as to the effect, if any, of the merger upon Western.

To meet the difficulties of delay and disruption of orderly procedure inherent in its proposal, Western, in its petition for reconsideration, has advanced various reasons in explanation and justification of its failure to file its route applications at an earlier date. Western argues that filing of its applications was done at a time and in a manner which in the light of historical developments was the earliest time when it was appropriate for Western to do so. This argument is based on the contention that it was not until the actual filing of merger plans between Southwest and West Coast that the full objective of their ambitions and its effect upon Western was revealed. As a part of this contention, Western alleges that for approxi-

mately a year, it has vigorously endeavored to achieve some Western-Southwest-West Coast merger, consolidation, or acquisition and that it would have been extremely unwise

[7]

for Western to have defeated any chances it might have had for successful completion of these negotiations by filing an application for the same points served by the companies involved. It may be noted that Southwest and West Coast deny that there was ever any serious negotiations between those companies and Western. However, even if the allegations of Western are given their full weight, it is apparent that they do not furnish a basis to change our previous determinations that the requested consolidation would cause undue delay and interfere with orderly procedure. Whatever the merits of Western's action or non-action from its own point of view, it is nevertheless clear that the carrier made a deliberate choice and must now abide by that choice. Western cannot now contend that the administrative clock should be set back in order to accommodate its late filing.

Western has also argued that Southwest and West Coast suppressed their merger plans during consideration of the renewal cases involving those carriers and that these plans were not smoked out until Western filed requests for subpoenas in the West Coast Case. It is argued that this constitutes a misleading circumstance which further explains why Western did not file its route applications at an earlier date. In a document filed on July 25,

1950, Western set forth various facts in support of its allegation based upon exhibits which have been submitted in the merger case. Even if there were any misrepresentation such as alleged, and we do not here pass on that point, it occurred long after the appropriate

[8]

time for Western to have filed its applications for authorization to serve Southwest and West Coast's routes in order to have them heard with the renewal proceedings.

Apart from this question of misrepresentation in the renewal proceeding, Western apparently assumes that during the pendency of negotiations between Southwest and West Coast, prior to the completion and filing of the merger agreement, Western was entitled to be advise of the status of such negotiations for the purpose of determining its course of action. It would seem obvious that no such right in Western exists.

In any event, we are not impressed with the atmosphere of conspiracy that Western seeks to create here. The possibility—or indeed the likelihood—of a proposal for merging the Southwest and West Coast systems has been obvious since the creation of these two carriers, and those familiar with the airline industry have long been aware of the possibility of such a development. The mere fact that Western may have been frustrated in its efforts to keep abreast of the merger negotiations between West Coast and Southwest does not mean that Western was thereby rendered powerless to protect its position. If Western feared the possibility of a merged feeder system



on the West Coast, and wished to combat it by a proposal for rendering the service itself, Western could and should have filed timely applications to compete with the renewal applications of West Coast and Southwest.

[9]

Without passing upon the various problems that must be explored in the merger case, and the additional impact that a merged system may have on Western's position, Western cannot escape the fact that the separate routes of West Coast and Southwest were in existence for approximately three years prior to the start of the renewal proceedings. When the Board proposed to renew these routes for an additional five-year period, not only did Western fail to file competing applications for the routes, but it did not for some time even oppose the proposed renewal of the routes.<sup>1</sup> It is thus apparent that Western has, for a considerable time, and to a considerable extent, slept on its opportunities to seek authority to supplant the West Coast and Southwest systems, and it is clear that its present concern is a product of its own course of conduct rather than any inequities in the Board's procedures.

[10]

United in its motion filed April 27, 1950, requested (1) severance from the Southwest and West Coast Renewal

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<sup>1</sup>It is of interest that Western did not even appear at the Pre-hearing Conferences in the renewal cases of either Southwest or West Coast. In the Southwest renewal case it was not until February 10, 1950,—after the hearing—that Western addressed a letter to the Examiner announcing Western's opposition to the renewal of Southwest's certificate. This late awakening or change of heart, as the case may be, is particularly noteworthy since the renewal cases involved the basic route structure that Western wishes to supplant by its own tardy route applications. The merger agreement, while providing for a single company to operate both feeder route systems, does not and cannot provide for any additional route authorizations (other than the possibility of single plane service rather than connecting plane service at Medford).



Cases of the issues of renewal of the certificates of Southwest and West Coast (leaving therein only the issues of suspension of United at certain of its points and substitution of Southwest and West Coast); (2) consolidation of the severed portions with the application of Southwest and West Coast for merger, for hearing and decision; (3) deferment of all further procedural steps with respect to the remainder of the Southwest and West Coast Renewal Cases, and deferment of the reopened Additional California-Nevada Service Case, until after final decision in the merger case and, in the event the merger is approved, until after operating experience has been obtained under the merger. This motion was denied by Order Serial No. E-4292 on the basis of the findings set forth therein.

In its petition for reconsideration of Order Serial No. E-4292 United argues for the first time that such order is erroneous and invalid as a matter of law in that it denies United the full and fair hearing required by *Morgan v. U. S.*, 304 U. S. 1. United contends that the Board's order does not give it a reasonable

[11]

opportunity to know and meet the present claims of the opposing parties in the renewal-suspension cases; that the Board has erroneously shifted upon United the burden of trying the effects of the merger upon the suspension-substitution issues in such cases; and that the Board must now come forward and show what changes, in its opinion, are required in its prior show cause orders initiating these cases if the merger is approved. We believe that the procedure provided in the Board's prior order fully meets the rights of United to full and fair hearing upon the suspension-substitution issues in the renewal-suspension cases in the light of the proposed Southwest-West Coast

merger. In that order we took cognizance of the possible effect of the merger proceeding on the suspension issues in the two renewal cases and ordered the reopening of Docket No. 3718 *et al.* and the reconvening of the proceeding in Docket No. 3966 for further hearing in order that evidence may be adduced with respect to the effect, if any, of the merger proposal upon such issues.

We have further established a schedule of hearings under which hearing before the Examiner in the merger case will be completed prior to the reopened and reconvened hearings in the renewal-suspension cases. United thus has full opportunity to present in the records of the renewal-suspension cases all relevant evidence as to the effects of the merger on the suspension-substitution issues. Moreover, it will have full opportunity to cross-examine on any evidence presented by Government counsel as to the effect of the proposed merger on the issues affecting United.

[12]

The carrier cannot insist that the orders instituting the renewal-suspension cases be amended and reissued and the proceedings in effect start over again because of the intervening fact of the proposed merger. All it is fairly entitled to is the right to explore in the record of those cases the effect of the merger, if any, upon the suspension-substitution issues. Recognition of an argument that the order instituting the proceedings must be amended to include subsequent intervening facts would make it impossible to complete such proceeding. Finally, the Board was not required to issue show-cause orders to initiate the renewal-suspension cases. It could have utilized an investigatory type of order. The fact that the Board gave United the benefit of its preliminary thinking in the form of show-

cause orders does not impose any greater burden on the Board or give United any greater rights that it would have otherwise had.

/s/ OSWALD RYAN

/s/ JOSH LEE

[1]

STATEMENT OF MEMBER JONES  
IN OPPOSITION TO THE ORDER,  
MEMBER ADAMS CONCURRING

The Board did on June 6, 1950, deny various motions and petitions of United Air Lines, Inc. (United) and Western Airlines, Inc. (Western), requesting that various related cases involving air transportation on the West Coast be consolidated into one proceeding.

United filed with the Board exceptions to the order denying its motion and also filed a petition for reconsideration of the order. Western likewise filed a petition for reconsideration.

These petitions for reconsideration duly came before the Board, together with the answers and replies of West Coast and Southwest in opposition thereto. The four members of the Board were equally divided on the question as to whether or not said petitions should be granted, and the Acting Chairman instructed the Secretary to prepare an order denying said petitions for want of a majority.

It must be presumed that the two members who voted to deny the petitions had proper grounds for doing so, to-wit: that (a) no new matters were presented by the petitioners; and (b) no legal question was raised, of sufficient importance to justify a reconsideration.

I cannot agree with the determination arrived at by my two colleagues. New matters of very large importance were called to the Board's attention by the petitioners, and serious questions of law were presented.

For example, there was called to the Board's attention the fact that West Coast and Southwest had actually signed a merger agreement prior to the hearing on the renewal of West Coast's certificate. I quote from United's pleadings:

[2]

"On November 6, 1949, West Coast's and Southwest's officials signed an agreement whereby the parties agreed to a merger plan between the two companies which had been in negotiation from prior to the time of the above testimony (Ex. S-14). On December 2, 1949, West Coast's Board of Directors approved the reorganization plan whereby West Coast would be merged into Southwest upon the terms set forth in the proposed merger agreement (Exs. S-12, S-14, S-15). Yet on March 28, 1950, West Coast's Executive Vice President testified in the *West Coast Renewal-United Suspension Case* that West Coast's Board of Directors had merely authorized West Coast's President to investigate the possibility of a merger and 'that is the extent of it so far. He has not reported back to the Board of Directors' (Rec. 299-300, Docket No. 3966, et al.)."<sup>1</sup>

United also called to the attention of the Board the conduct of counsel for Southwest at the same hearing, which

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<sup>1</sup>Reply of United Air Lines, Inc., to the Answer of West Coast Airlines and Southwest Airways to United's and Western's Petitions for Reconsideration, July 20, 1950; page 5.



conduct, to put it euphemistically, was evasive and misleading, and, from the record, an apparent effort to conceal that a merger agreement between Southwest and West Coast did in fact exist.<sup>2</sup>

Western raised a serious question of law in urging, with impressive force, that judicial precedents require the Board to consolidate Western's applications for the West Coast feeder routes into the pending renewal proceedings for concurrent decision. The legal issue thus presented is an important one, and in itself should require reversal of the Board's previous order of denial.<sup>3</sup>

Numerous other instances of new matters called to the attention of the Board could be cited. The above should suffice.

[3]

Under these circumstances the Board was called upon to make a determination whether to review these matters, together with the other matters discussed *infra*, in one proceeding in a logical effort to, with the broadest possible freedom, attempt to determine the overall air transport needs of this very important area at one time, with all the related facts and issues before it. The alternative was to ignore basic and important issues directly affecting the welfare of the entire West Coast and the air transport system best fitted to serve this area, and determine the issues on a case-by-case basis in what would amount to a succession of "keyhole" approaches limited as to issues and scope of possible action.

The pending route cases include the *Southwest Renewal-United Suspension Case*, Docket No. 3718, *et al.*, which

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<sup>2</sup>*Ibid.*, page 6.

<sup>3</sup>Petition of Western Air Lines, Inc., for Reconsideration, June 26, 1950; page 23 *et seq.*



involves the future of Southwest and the feeder service pattern in the area in which it operates; the *West Coast-United Suspension Case*, Docket No. 3966, *et al.*, which presents the same issues with respect to West Coast and its operating territory; and the *Reopened Additional California-Nevada Service Case*, Docket No. 2019, *et al.*, concerning the air service pattern in the area between Los Angeles and San Diego, on the one hand, and Phoenix on the other. These cases have been pending for some time, hearings have been held, and the Examiner's report has been issued in the Southwest Renewal Case.

These issues alone should justify the consolidation requested. However, they have been greatly broadened as a result of the filing on April 10, 1950, of a request for the approval of the proposed merger between Southwest and West Coast above mentioned. As stated before, West Coast and Southwest apparently sought to conceal the proposed merger from the Board until

[4]

after the prospective renewal cases had been decided, and it was only brought to the Board's attention as a result of a threat of subpoena.

A merger of so-called feeder lines of the magnitude revealed by the merger agreements and the record raises very important matters of policy directly affecting the air transport system on the West Coast and indirectly affecting the entire domestic air transport system. It directly poses the question asked by me in the *Monarch-Arizona Merger Case*,<sup>4</sup> which question remains unanswered by the Board, namely:

"What is the feederline experiment *now* being con-

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<sup>4</sup>Docket No. 3977, *et al.*, decided April 10, 1950.

ducted by the Board—is it the establishment of a secondary nationwide system to be perpetually subsidized by the Government to the extent of many millions of dollars per year, or is it controlled experimentation with a number of supplemental local systems which give some promise of achieving self-sufficiency?”

This important question might well be answered by action taken by the Board in a consolidated proceeding, because this merger proposal, together with the other matters in issue, raises the possibility of a single, secondary, short-haul “feeder” system extending the length of the West Coast and penetrating the Southwest as far as Phoenix, Arizona. It, together with the huge feeder system created by the Monarch-Challenger-Arizona merger, may well serve to establish a secondary subsidized feeder system embracing the entire western United States. Surely, the public and other interested airlines have the right to have this matter considered in connection with the *Southwest Renewal-United Suspension Case* in which the Board has tentatively decided to renew Southwest’s certificate and attempt to give portions of United’s system to it; and the *West Coast-United Suspension Case* which

[5]

likewise proposes to renew West Coast and again to give certain of United’s system to it; and the other related matters sought to be consolidated by the Petitioners.

Surely, if the Board does intend to create a secondary nationwide system serving smaller communities and perpetually subsidized by the government, the taxpayer is entitled to be apprised of its intention. It should not creep upon the matter by stealth and create such a system piece-

meal. If the traveling public and shippers in the smaller cities are to be furnished by the government with a kind of social service whereby transportation is to be furnished to the citizens dwelling in the smaller cities cheaper than its cost, then the taxpayer should be entitled through Congress to know what the cost will be and whether *all* the people want it.

There is also pending a Board investigation into the route structure of Western, Docket No. 2911, which was launched by the Board in February, 1949, because it appeared to be an area where "remedial action designed to correct uneconomic situations is desirable."<sup>5</sup> Although the Western investigation has not been actually processed to date, the Board has informed the public that "it will be pushed forward as rapidly as staff permits."<sup>6</sup>

Thus, it seems to me that the Board has been presented by the West Coast carriers with a perfect opportunity to proceed with the final determination of the service required by the public interest and at the same time to complete the investigation which it inaugurated.

[6]

It seems particularly indefensible to refuse to hear the applications of Western for the operation of the West Coast feeder routes before deciding the applications of West Coast and Southwest for certificate renewal and approval of the merger proposal. This amounts in practical effect to a refusal to hear issues which offer the prospect of saving the taxpayer at least \$750,000 annually, even though it would involve no disruption of present service or substantial prejudice to any carrier. If the

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<sup>5</sup>*Statement of Policy* from Economic Program for 1949, p. 14.

<sup>6</sup>*Annual Report of Civil Aeronautics Board*, 1949, p. 6.

Southwest and West Coast certificates are renewed, and their proposed merger is approved, then it is perfectly obvious that Western's proposal will, as a practical matter, have been foreclosed. In addition to the important public interest elements involved, such a procedure poses serious legal questions which should be carefully considered, rather than disposed of in so cavalier a manner.

Under all the circumstances, I feel that both the public interest and the interests of all the parties demand that the Board's previous denial of the petitions of United and Western should be reconsidered and reversed and that all of the pending proceedings involving West Coast service, including the Western investigation, should be consolidated, in order that the Board might hear all of the facts and all of the issues before deciding the future of the West Coast air transport system.

Member Adams joins me in this Statement.

/s/ HAROLD A. JONES

/s/ RUSSELL B. ADAMS

## Orders

Serial Number E-4484

[1]

UNITED STATES OF AMERICA  
CIVIL AERONAUTICS BOARD  
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board  
at its office in Washington, D. C.,  
on the 26th day of July, 1950.

- - - - - :  
In the matter of the :  
SOUTHWEST-WEST COAST :  
MERGER APPLICATION :



SOUTHWEST RENEWAL-UNITED:	
SUSPENSION CASE	:
WEST COAST RENEWAL-	:
UNITED SUSPENSION CASE	:
REOPENED ADDITIONAL	:
CALIFORNIA-NEVADA	:
SERVICE CASE	:
WESTERN AIR LINES, INC.	:
Application for additional in-	Docket Nos. 4405
intermediate points in the	3718 <i>et al.</i>
states of California, Oregon	3966 <i>et al.</i>
and Washington on its Route	2019 <i>et al.</i>
63,	4447
WESTERN AIR LINES OF THE	4448
PACIFIC, INC.	4449
Application for a certificate	:
of public convenience and	:
necessity for a route between	:
Los Angeles, California and	:
Bellingham, Washington by	:
way of various intermediate	:
points, and	:
WESTERN AIR LINES, INC.	:
Application for approval of	:
the acquisition of complete	:
stock ownership of Western	:
Air Lines of the Pacific, Inc.	:
- - - - -	- - - - -



ORDER.

The Board having by Order Serial No. E-4292, dated June 6, 1950, acted upon various motions and petitions of United Air Lines, Inc. (United), Western Air Lines, Inc. (Western), and Southwest Airways Company (Southwest), requesting, *inter alia*, certain severances, consolidations, and deferrals;

United having filed with the Board on June 22, 1950, exceptions to, and a petition for reconsideration of Order Serial No. E-4292;

Western having also filed with the Board on June 26, 1950, a petition for reconsideration of the aforementioned order;

West Coast Airlines, Inc. (West Coast) and Southwest Airways Company (Southwest), having filed with the Board on July 14, 1950, a joint answer to the aforementioned petitions for reconsideration; and United and Western having filed replies to the aforesaid answer;

[2]

The Board having duly considered the aforementioned petitions, answer, and replies, and the four members of the Board being equally divided on the question whether such petitions should be granted, the petitions fail for want of a majority;

IT IS THEREFORE ORDERED, That the aforementioned petitions for reconsideration filed by United and Western be and hereby are denied.

By the Civil Aeronautics Board:

/s/ Fred A. Toombs  
Fred A. Toombs  
Acting Secretary

(SEAL)

No. 12639

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United States  
Court of Appeals  
for the Ninth Circuit.

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COMMISSIONER OF INTERNAL REVENUE,  
Petitioner,

vs.

BIRCH RANCH AND OIL COMPANY,  
Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States

**FILED**

OCT 30 1950

**PAUL P. O'BRIEN,**  
CLERK



No. 12639

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United States  
Court of Appeals  
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## INDEX

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## Appearances

For Petitioner:

GEORGE ACRET, ESQ.

For Respondent:

EARL C. CROUTER, ESQ.

## DOCKET ENTRIES

1945

July 13—Petition received and filed. Taxpayer notified. Fee paid.

July 13—Copy of petition served on General Counsel.

July 25—Amended petition filed by taxpayer. Copy served 7/25/45.

July 30—Entry of appearance of George Acret as counsel filed.

Aug. 29—Answer filed by General Counsel.

Aug. 29—Request for hearing in Los Angeles, Calif., filed by General Counsel.

Aug. 31—Notice issued placing proceeding on Los Angeles, Calif., calendar. Service of answer and request made.

1946

Dec. 6—Hearing set Feb. 10, 1947, at Los Angeles, Calif.

1947

Jan. 31—Motion for extension of time to the next Los Angeles, calendar filed by petitioner. Granted 1/31/47.

Apr. 24—Hearing set 6/23/47—Los Angeles.



1947

June 30—Hearing had before Judge Kern on merits.

Briefs due 8/14/47. Replies due 8/29/47.

July 22—Transcript of hearing 6/30/47 filed.

July 29—Motion for extension to 8/31/47 to file brief filed by taxpayer 7/30/47 Granted.

Aug. 14—Brief filed by General Counsel.

Sept. 2—Brief filed by Taxpayer 9/3/47 copy served.

1948

Mar. 24—Memorandum findings of fact and opinion rendered. Kern—J. Decision will be entered for the Respondent 3/24/48. Copy served.

May 21—Motion to reopen case filed by Petitioner.

May 26—Order—granting petitioners motion to reopen case for further hearing—proceeding to be set at Los Angeles first calendar after 7/1/48—entered.

July 28—Hearing set October 11, 1948. Los Angeles, Calif.

Oct. 11—Hearing had before Judge Arundell, Petitioner's oral motion for continuance, motion for leave to amend pet. Motion granted. Continued to next calendar subsequent to Nov. 1948. 30 days leave granted to file amended petition. Respdt. allowed 15 days to answer.

Oct. 11—Order that the proceeding is continued to the next Los Angeles calendar subsequent to 11/29/48 entered.

Nov. 4—Transcript of hearing 10/11/48 filed.

1948

Nov. 12—Supplement and amendment to petition filed by petitioner. 11/12/48 copy served.

Dec. 1—Answer to petitioner's supplement and amendment to petition filed by respondent. 12/2/48 copy served.

Dec. 23—Hearing set Feb. 7, 1949, Los Angeles.

1949

Feb. 11-15—Hearing had before Judge Johnson on merits, petitioner's oral motion to amend petition and respondent's oral motion to amend answer—motions granted. Stipulation of facts, petitioner's trial memo of points and authorities, amendment to supplement and amendment to petition attached in file—copy served. Answer to second supplement and amendment to petition—copy served, petitioner's counsel's oral argument at hearing accepted as original brief. Respondent's brief 4/6/49—petitioner's reply brief 5/6/49.

Mar. 8—Transcript of hearing 2/11/49 filed.

Mar. 8—Transcript of hearing 2/15/49 filed.

Apr. 4—Motion for extension to 5/6/49 for respondent reply—and 30 day extension for pet.'s reply filed by General Counsel, 4/5/49 Granted.

May 2—Stipulation to correct transcript of record filed.

May 6—Brief filed by General Counsel.

1949

May 20—Motion for extension to June 26, 1949, to file reply brief filed by taxpayer. 5/25/49  
Granted.

Dec. 15—Findings of fact and opinion rendered.  
Johnson J. Decision will be entered under Rule 50—copy served.

1950

Jan. 24—Respondent's computation for entry of decision filed.

Feb. 8—Hearing set March 1, 1950, Wash., D. C., under Rule 50.

Mar. 1—Hearing had before Judge Disney on settlement—referred to Judge Johnson (Uncontested).

Mar. 3—Decision entered, Johnson J. Div. 10.

May 19—Petition for review by U. S. Ct. of Appeals for the 9th circuit and statements of points filed by General Counsel.

May 31—Proof of service of petition for review filed, on taxpayer and counsel for taxpayer.

June 19—Motion for extension of time to Aug. 17, 1950, to prepare and transmit the record filed by General Counsel.

June 19—Order enlarging the time to Aug. 17, 1950, to prepare and transmit the record entered.

July 6—Agreed notice of record on review filed.

Before  
The Tax Court of the United States  
Docket No. 8720

BIRCH RANCH & OIL COMPANY, a Corpora-  
tion,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiencies set forth by the Commissioner of Internal Revenue in Notice of Deficiency and Statement, L. A.: T.: 90D: P. B., dated April 30, 1945, and alleges as follows:

I. Petitioner is a corporation organized and existing under the laws of the State of Nevada with its principal office at 427 West Fifth Street, Los Angeles, California. The returns for the periods here involved were filed with the Collector of Internal Revenue for the Southern District of California at Los Angeles, California.

II. The said Notice of Deficiency and Statement, a copy of which is hereto attached marked "Exhibit A," was mailed to the petitioner on April 30, 1945.

III. The taxes in controversy are income and excess profit taxes for the fiscal years ending Sep-

tember 30, 1941, and September 30, 1942, and involve amounts as follows:

Year Ended	Liability	Assessed	Deficiency
	Income Tax		
9/30/41	\$ 7,833.44	None	\$ 7,833.44
9/30/42	11,915.67	None	11,915.67
Total	<u>\$19,749.11</u>	None	<u>\$19,749.11</u>
	Declared Value Excess-Profits Tax		
9/30/41	\$ 4,565.41	None	\$ 4,565.41
9/30/42	1,687.10	None	1,687.10
Total	<u>\$ 6,252.51</u>	None	<u>\$ 6,252.51</u>

The entire deficiency is in controversy for each of said years. Also, as hereinafter shown, petitioner is entitled to credits which would in any event offset the whole of such deficiency for each of said years.

IV. The determination of the taxes set forth in said notice of deficiency is based upon the following errors of the Commissioner:

(a) In holding that the petitioner's net income for both of said fiscal years is determined upon the cash receipts and disbursements basis, when in fact the petitioner's net income, since its organization on October 15, 1934, at all times has been and is determined upon an accrual basis of accounting.

(b) In disregarding the inventories covering petitioner's Conaway Ranch for each of said fiscal years upon the theory that the net income of said ranch is determined upon the cash receipts and disbursements basis, when in fact the net income of said ranch, and petitioner's entire system of



accounting, at all times has been and is determined upon an accrual basis.

(c) In holding that the income of petitioner's Etiwanda Citrus Ranch, and its system of accounting, for each of said fiscal years is upon the cash receipts and disbursements basis, when in fact the net income of said ranch, and petitioner's entire system of accounting, at all times has been and is determined upon an accrual basis.

(d) In disallowing petitioner's deduction for the year ending September 30, 1941, in the sum of \$120,000.00, except as to \$19,200.00 thereof, upon the theory that the same represents interest, when in fact the whole of such item of deduction represents, and is properly deductible as, taxes accrued to pay interest on \$2,000,000.00 of bonds issued by Reclamation District No. 2035, the principal of all of which bonds, with interest thereon, until paid constitutes a lien against petitioner's lands, and which interest accrues semi-annually as a lien and tax against petitioner's lands irrespective of the occurrence of any other event.

(e) In disallowing petitioner's deduction for the year ending September 30, 1942, in the sum of \$120,000.00, except as to \$19,200.00 thereof, upon the theory that the same represents interest, when in fact the whole of such item of deduction represents, and is properly deductible as, taxes accrued to pay interest on \$2,000,000.00 of bonds issued by Reclamation District No. 2035, which interest accrues semi-annually as a lien and tax against peti-

tioner's lands irrespective of the occurrence of any other event.

(f) In disallowing petitioner's net operating losses deducted by it in its income tax returns for the said taxable years ending September 30, 1941 and 1942, under the theory that such losses are not deductible under the provisions of Section 122 of the Internal Revenue Code.

(g) In disallowing the petitioner's deductions in its said income tax returns for each of said years for declared value excess profits for the erroneous reason that petitioner's net income is determined upon the cash receipts and disbursement basis when in fact, such net income is determined upon an accrual basis.

V. The facts upon which the petitioner relies as a basis for this proceeding are as follows:

(a) Petitioner was organized as a corporation on October 15, 1934; that at the time of its organization, petitioner adopted a fiscal year commencing on October 1 and ending on September 30, and a system of accounting upon an accrual basis; that petitioner has not since changed said fiscal year or its said system of accounting; that ever since said date of organization the petitioner has entered upon its books of account all accounts receivable and accounts payable when and as the same accrued and made its income tax returns upon said accrual basis of accounting. That the Commissioner has nevertheless disallowed the various items as set forth in said deficiency notice and statement (hereto at-

tached as Exhibit "A"), and as hereinafter referred to, upon the erroneous theory that petitioner's system of accounting is upon a cash basis.

(b) Ever since its said date of organization petitioner has owned and operated a ranch known as the Conaway Ranch; that all transactions concerning the operation of said ranch have been entered in a separate set of books; that at the time of petitioner's organization it adopted an accrual system of accounting for the said ranch and petitioner has not since changed its said system of accounting; that ever since said date petitioner has entered upon its books of account concerning said ranch all accounts receivable and all accounts payable when and as the same accrued and the petitioner has determined its net income from said ranch and all of its net income upon said accrual basis of accounting. That the Commissioner has nevertheless disallowed the various items relating to said Conaway Ranch as set forth in said deficiency notice and statement (hereto attached as Exhibit "A") upon the theory that this petitioner's system of accounting with relation to said ranch is upon a cash basis.

(c) Ever since its said date of organization petitioner has owned and operated what is known as the Etiwanda Citrus Ranch; that at the time of petitioner's organization it adopted an accrual system of accounting for the said ranch and petitioner has not since changed its said system of accounting; that ever since said date petitioner has entered upon its books of account concerning said ranch all accounts receivable and all accounts payable when

and as the same accrued and the petitioner has determined its net income from said ranch and all of its net income upon said accrual basis of accounting; that the Commissioner has nevertheless treated this petitioner's system of accounting as if said system with relation to said ranch were upon a cash basis.

(d)1. Ever since prior to the year 1872 it has been the policy of the State of California to encourage the development of marginal and undeveloped swamp and overflowed lands by providing for the formation of reclamation districts, constituting municipal corporations as separate legal entities, and by providing for the financing of such districts by the issuance of reclamation bonds with liberal payment and tax exemption privileges, and other privileges, and by providing that the principal and interest of such bonds shall constitute a first and prior lien until paid upon all of the lands of such districts.

2. In reliance upon the said policy and the laws of said State for the encouragement of the development of said marginal lands, the petitioner's predecessors in interest in the ownership of the said Conaway Ranch and other owners of land in the vicinity thereof, on or about April 8, 1919, caused to be created and said lands to be included in Reclamation District No. 2035 of the State of California; that said reclamation district consists of approximately 22,000 acres located in Yolo County, California, and it ever since has been and now is



a bona fide duly organized and existing reclamation district of said State.

3. At the said time of said organization of said district the landowners of said district transferred by deed to said district, rights of way and lands for roads, levees, ditches, pumping plants and warehouses, hereinafter referred to as said property; that said district as a separate entity ever since has been and now is the owner of said property.

4. Commencing immediately after the formation of said district the said district caused said property to be improved by the construction of approximately forty-five miles of roadways, forty-seven miles of irrigation canals, fifty-five miles of drainage canals and ditches, together with bridges, pumping plants, warehouses and other structures usual and necessary for the development and operation of such a district; that said improvements were completed prior to 1925 at a cost slightly in excess of the sum of \$2,000,000.00.

5. In order to pay for the cost of said improvements and pursuant to the provisions of Section 3457 of the Political Code of the State of California, the said district duly caused to be issued a bond issue in the sum of \$2,000,000.00 covering all of the lands of said district; that said bonds are each dated January 21, 1925, and each bear interest at the rate of 6% per annum, payable on the 1st day of January and the 1st day of July of each and every year until paid, and said bonds mature each year in series commencing on the 1st day of



January, 1935, up to and including January 1st, 1943; that under the laws of said State the said interest accrues in the manner aforesaid and becomes a tax lien against the petitioner's land irrespective of any act of said Reclamation District or of any call by the County Treasurer, and said interest remains a tax lien upon the whole of petitioner said Conaway Ranch until paid.

6. Between 1925 and 1934 two of petitioner's predecessors in interest, to wit: A. Otis Birch and wife, acquired the title to the whole of the said Conaway Ranch and they also acquired all of the other parcels of land comprising said district, except one small parcel, and caused such additional parcels so acquired to be and become a part of said Conaway Ranch; that between said dates said Birch and wife also acquired the ownership of a large majority of said bonds; that ever since 1934 except for said one parcel of land, and except for said property of said district, said Conaway Ranch has comprised the entire area of said district.

7. With respect to their income tax returns for each year between 1925 and 1934 said Birch and wife adopted the practice of deducting, and they did deduct, said item of \$120,000.00 as taxes, the same representing an amount sufficient to pay the total annual interest accruing upon said \$2,000,000.00 of bonds; also in said income tax returns for each of said years said Birch and wife did not account for or include as part of their gross income, any part of the interest received by them from any of said bonds upon the theory that such income was

exempt from taxation under the laws of the State of California.

8. The Commissioner questioned each of said deductions for each of said years and said failure to include said income from said bonds, and in each instance, after investigation and consideration, the Commissioner approved each of said deductions and said failure to include said income.

9. Ever since the said development of said district said Conaway Ranch has been operated as a farm in the raising of rice and sheep and other farm products. Such operations require current financing in a sum substantially in excess of \$100,000.00 per year. After the commencement of the depression in 1929, A. Otis Birch and wife found it inconvenient to advance such current financing and they found it necessary and desirable to borrow money for such purpose. On attempting so to do, they found it then was the policy of all financial institutions not to loan such sums of money to individual persons and that it was impossible for them to borrow any substantial sum from such institutions, or at all, unless they should place a substantial part of their property in a corporate form of ownership.

10. Solely for the purpose of obtaining said current financing, and other financing, and for the purpose of enjoying the legitimate advantages of a corporate form of organization, said Birch and wife caused the petitioner herein to be incorporated on the 15th day of October, 1934, in the State of Nevada. On the same date and for the same reasons

and as part of a convenient corporate set-up for the proper segregation of their properties, they also caused to be incorporated the Birch Securities Company, a corporation of the State of Nevada, and the Birch Holding Company, a corporation of the State of Delaware. Said Birch and wife thereupon transferred all of the aforesaid bonds owned by them to said Birch Securities Company and the whole of said Conaway Ranch, together with a portion of all other properties owned by them, to the petitioner herein. The petitioner and said Birch Securities Company thereupon issued all of their respective authorized capital stock and transferred the same to the Birch Holding Company and said Birch Holding Company thereupon issued all of its capital stock and transferred 49% thereof to A. Otis Birch and 51% thereof to M. Estelle C. Birch, his wife, each of which persons owned all of said capital stock during the fiscal years involved herein.

11. The organization of all of said companies was made in good faith and was bona fide in every respect and said organization was not made with a view to affecting in any manner the obligation of said Birch and wife, or of any of said companies, to pay taxes of any kind or character, nor was it made for the purpose of enabling petitioner to take the deductions involved herein for taxes paid to said reclamation district, since the said Birch and wife for approximately eight years prior to the organization of said companies had been after full consideration by the Commissioner, as aforesaid,

permitted to take said deductions from their income tax returns for each of said years.

12. Since its incorporation the petitioner has borrowed various sums of money from various banks and other financial institutions to the extent of substantially in excess of \$100,000.00 a year. The petitioner has ever since its organization engaged in the business of operating said ranch and of developing oil wells and other enterprises as a separate legal entity separate and apart from the activities and obligations of said Birch and wife and of said other companies. Ever since its organization petitioner has had its separate creditors, separate and apart from said Birch and wife and said other companies, and said financial institutions and various other creditors have extended credit to the petitioner in reliance upon the fact that the petitioner is a separate corporate entity which is responsible for the payment of no obligations, including taxes, other than its own.

13. Petitioner is in fact a separate legal and corporate entity and it is not in any respect the alter ego of said Birch and wife or of said other corporations, or any of them, or of any other person or corporation, and its organization, and the afore-said set-up, are legitimate and bona fide in every respect.

14. On October 15, 1934, the ownership of said bond issue was as follows:



Republic Life Insurance Company.....	\$ 86,000.00
Lula M. Minter.....	10,000.00
The Hopkins .....	309,000.00
A. Otis Birch and wife.....	1,595,000.00
<hr/>	
Total .....	\$2,000,000.00

15. That during 1941 and 1942 the ownership of said bonds was as aforesaid except that the Birch Securities Company on October 15, 1934, acquired the aforesaid bonds owned by A. Otis Birch and wife, of the said face value of \$1,595,000.00, and except that in 1940 this petitioner acquired said bonds owned by said Republic Life Insurance Company of the face value of \$86,000.00; that except as aforesaid, this petitioner has not owned, and does not now own, any of said bonds.

16. On October 6, 1934, an election was duly held in said Reclamation District No. 2035 for the refunding of all said bonds, pursuant to the provisions of said Section 3480. At said election the issuance of 2,000 new bonds in the place of said old bonds was duly authorized. Said new bonds mature as stated in said Notice of Election and they are in like number and amount as said old bonds and they likewise bear interest at 6% to the end that such new bonds when issued take the place of said old bonds and to the end that interest upon the entire principal of said bond issue is continuous and a first and prior lien against all of the lands of the said district until said bonds are paid.

17. On or about 1942 said new bond issue was



issued in the place of said old bonds. Pursuant to the provisions of said Section 3480 the said lands are subject to a lien of continuously accumulating interest at said rate of 6%, whether said interest accrues from said old bonds or said new bonds, and until said sum of \$2,000,000.00 is paid that all of said bonds are outstanding and unpaid.

18. Since 1925 the petitioner and its said predecessors in interest, in exchange for the use of said property of said district, including said warehouses, has paid all expenses for the operation of said district, so that the only expense which said district has and for which it need raise any taxes is the payment of said interest on said bonds in the sum of \$120,000.00 per year. By reason of these facts the amount of said Reclamation District tax against petitioner's land is exactly said sum of \$120,000.00 a year, which sum accrues solely by reason of the existence of said bonds and irrespective of the occurrence of any other event.

19. That at all times since its said organization petitioner has paid in cash to the County Treasurer of said Yolo County, or to the bondholders of said bond issue in exchange for an equivalent amount of interest coupons of said bonds, an amount of money or interest coupons sufficient to pay the taxes to meet the interest upon all of said bonds promptly as such interest became due, except that from 1936, up to and including the year 1940, this petitioner did not pay the amount of money necessary to meet the interest coupons as the same accrued upon the

aforesaid bonds owned and held by said Birch Securities Company; that petitioner did not make said payments for the reason, among others, that in 1937 the Birch Securities Company became, and ever since has been, suspended by the Franchise Tax Commissioner of the State of California for alleged non-payment of certain California State Franchise taxes; that under the laws of the State of California, the said Birch Securities Company, during the existence of said suspension until 1941, was prohibited from delivering any of the interest coupons of said bonds owned by it, or from accepting any money therefor under penalty of a criminal prosecution, a severe fine, and possible imprisonment of its officers; that on June 9, 1941, said Birch Securities Company, through its president, A. Otis Birch, in an action entitled, A. Otis Birch vs. Charles J. McColgan, as Franchise Tax Commissioner of the State of California, the same being cause No. 1430B of the District Court of the United States for the Southern District of California, received an opinion from said court, sitting as a three-judge statutory court, to the effect that said suspension of Birch Securities Company was wrongful and void (39 Fed. Supp. 358); that thereafter a permanent injunction was issued by said three-judge statutory court prohibiting said Franchise Tax Commissioner from maintaining said suspension; that thereafter other obstacles which had prevented this petitioner from obtaining said coupons from said Birch Securities Company also became removed, and thereafter, to wit: commencing

prior to October 1, 1943, and including the whole of the said fiscal years involved herein, this petitioner commenced to pay money sufficient to meet the interest on all of said bonds, including the said bonds of the said Birch Securities Company; that in every instance where this petitioner has paid money directly to said bondholders in exchange for interest coupons of said bonds, this petitioner has deposited said interest coupons with the County Treasurer of said county as the equivalent of money for the payment of said taxes; that the laws of the State of California permit and expressly provide that the taxes of a reclamation district may be paid in such manner.

20. Upon its books of account, petitioner included, for its fiscal year ending September 30, 1941, items of interest payable and paid on said bonds as taxes to said district in the sum of \$120,000.00. In its income tax return for said year, petitioner deducted said sum of \$120,000.00 as taxes accrued. Said deduction is a proper item of deduction for said purpose. Notwithstanding the facts aforesaid, the Commissioner erroneously disallowed said item in said Notice of Deficiency and Statement.

(e)1. Petitioner hereby incorporates paragraphs (d)1 to (d)20 hereof as part of this paragraph.

2. Upon its books of account, petitioner included for the fiscal year ending September 30, 1942, items of interest payable and paid on said bonds as taxes to said district in the sum of \$120,000.00 In its

income tax return for said year, petitioner deducted said sum of \$120,000.00 as taxes accrued. Said deduction in a proper item of deduction for said purpose. Notwithstanding the facts aforesaid, the Commissioner erroneously disallowed said item in said Notice of Deficiency and Statement.

(f)1. Petitioner hereby incorporates paragraphs (d)1 to (d)20 hereof as part of this paragraph.

2. That in its income tax returns for the years ending September 30, 1941 and 1942, the petitioner deducted operating losses in the sums of \$184,085.69 and \$143,714.15, respectively, as shown by the Commissioner's said Notice of Deficiency and Statement; that said operating losses, and each and every item thereof, were actual operating losses and proper items of deduction; that notwithstanding the facts aforesaid the Commissioner disallowed all of said operating losses upon the erroneous theory that petitioner's net income is determined upon the cash receipts and disbursements basis when in fact said net income should have been and is determined upon said accrual basis.

(g)1. Petitioner hereby incorporates paragraphs (d)1 and (d)20 hereof as part of this paragraph.

2. That by reason of the facts aforesaid, in its said income tax returns for the years ending September 30, 1941 and 1942, the petitioner made no declared value of excess profit tax assessed; that notwithstanding the facts aforesaid the Commissioner in said Notice of Deficiency and Statement erroneously assessed against this petitioner a deficiency of declared value excess profit taxes in the



sums of \$4,565.41 and \$1,687.10, respectively, upon the erroneous theory that petitioner's net income is determined upon the cash receipts and disbursements basis when in fact said net income should have been and is determined upon said accrual basis.

(h) That during petitioner's fiscal year ending September 30, 1943, petitioner suffered a loss by reason of non-payment of a loan made by it to the Birch-Smith Storage Company, a California corporation, operated and owned independently of said A. Otis Birch and wife, in the sum of \$52,031.26; that during said year petitioner also suffered a loss of a loan made to one Edna Tiller in the sum of \$200.00; that during said year petitioner also suffered a loss by reason of an unpaid loan made to Mrs. A. E. Dye; that in its income tax return for said year, petitioner listed and deducted said items of loss in the total sum of \$52,481.26; that should this court deny any part of this petitioner's petition herein, this petitioner desires to carry back to its fiscal years ending September 30, 1941 and 1942, as much of said sum of \$52,481.26 up to \$12,000.00 thereof, as may be necessary to offset any part of the said tax deficiencies involved herein.

(i) That during petitioner's fiscal year ending September 30, 1944, petitioner suffered a loss in the sum of \$73,556.88 by reason of the drilling and abandonment of an oil well known as the Stovall-Wilcoxson well, and the leasehold interest in connection therewith; that in the same year this



petitioner suffered losses from sales of property other than capital assets as follows:

A 338-acre farm situated in Stanislaus

County, California .....	\$36,417.50
Lots 61, 112, 141, Tract 993.....	1,160.00
Lots 32, 36, 60, 91, Tract 993.....	1,520.00
Lots 87, 62, 189, 90, 108, Tract 993.....	1,730.00
Lot 201, Tract 993.....	1,200.00
Store Building, 320 Venice Blvd., Los Angeles .....	5,500.00

that in its income tax return for said year petitioner listed and deducted all of the aforesaid items of loss in the total sum of \$121,084.38; that should this court deny any part of this petitioner's petition herein this petitioner desires to carry back to its fiscal year ending September 30, 1942, as much of said losses in the said sum of \$121,084.38, up to \$25,000.00 thereof, as may be necessary to offset any part of the said tax deficiencies involved herein.

Wherefore, petitioner prays that this court hear this proceeding and that the petitioner be granted relief as follows:

(a) That this court adjudge and declare that this petitioner's net income, and its system of accounting, for said fiscal years ending September 30, 1941 and 1942, and for all years, has been and is determined upon an accrual basis.

(b) That this court adjudge and declare that this petitioner's net income, and its system of accounting relating to said Conaway Ranch for each of said years, and for all years, is determined upon an accrual basis.

(c) That this court adjudge and declare that this petitioner's net income, and its system of accounting, relating to said Etiwanda Citrus Ranch, for each of said years, and for all years, is determined upon an accrual basis.

(d) That this court determine that the petitioner is entitled to a deduction in the full sum of \$120,000.00, accrued as taxes for payment of interest upon bonds of Reclamation District 2035 of the State of California for the fiscal year ending September 30, 1941.

(e) That this court determine that the petitioner is entitled to a deduction in the full sum of \$120,000.00, accrued as taxes for payment of interest upon bonds of Reclamation District 2035 of the State of California for the fiscal year ending September 30, 1942.

(f) That this court determine that this petitioner is entitled to deduct the operating losses as deducted by it in its income tax returns for the said taxable years ending September 30, 1941 and 1942, and as disallowed by the Commissioner in said Notice of Deficiency and Statement.

(g) That this court determine that this petitioner's failure to include in its said income tax returns for each of said years any declared value excess profits is proper, and that the Commissioner's assessed deficiencies therefor, are erroneous and improper.

(h) That should this court deny any part of this petitioner's petition herein that petitioner be adjudged entitled to carry back to its fiscal years

ending September 30, 1941 and 1942, as much of said sum of \$52,481.26, up to \$12,000.00 thereof, as may be necessary to offset any part of the said tax deficiencies involved herein.

(i) That should this court deny any part of this petitioner's petition herein that petitioner be adjudged entitled to carry back to its fiscal year ending September 30, 1942, as much of said losses in the said sum of \$121,084.38, up to \$25,000.00 thereof, as may be necessary to offset any part of the said deficiencies involved herein.

(j) That this court disallow and redetermine all of the said deficiencies as determined by the Commissioner in said Notice of Deficiency and Statement.

GEORGE ACRET,

/s/ GEORGE ACRET,

Attorney for Petitioner.

State of California,

County of Los Angeles—ss.

R. R. Landrum, being duly sworn, says that he is the Secretary of the petitioner and that he is duly authorized to verify the foregoing petition in behalf of the petitioner; that he has read the foregoing petition and is familiar with the statements contained therein and that all of the statements contained therein are true except those stated to be upon information and belief, and all of such statements he believes to be true.

R. R. LANDRUM.

/s/ R. R. LANDRUM.

Subscribed and sworn to before me this 10th day of July, 1945.

[Seal]      /s/ GEORGE ACRET,  
Notary Public in and for the County of Los Angeles, State of California.

Exhibit "A"

Form 1279

[Emblem]

Office of

Internal Revenue Agent in Charge

Los Angeles Division

LA:IT:90D:PB.

Treasury Department  
Internal Revenue Service,  
417 South Hill Street,  
Los Angeles 13, California

Apr. 30, 1945.

Birch Ranch & Oil Co.,  
427 West 5th Street,  
Los Angeles 13, California.

Gentlemen:

You are advised that the determination of your income tax liability for the taxable years ended September 30, 1941 and 1942, disclose a deficiency of \$19,749.11, and that the determination of your declared value excess-profits tax liability for the taxable years mentioned discloses a deficiency of \$6,252.51, as shown in the statement attached.

In accordance with the provisions of existing in-



ternal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Los Angeles, California, for the attention of LA:Conf. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,

Commissioner,

By GEORGE D. MARTIN,  
Internal Revenue Agent  
in Charge.

Enclosures:

Statement

Form of waiver



Statement

LA:IT:90D:PB

Birch Ranch & Oil Co.  
427 West 5th Street  
Los Angeles 13, California

Tax Liability for the Taxable Years  
Ended September 30, 1941, and September 30, 1942

Year Ended	Liability	Assessed Income Tax	Deficiency
9/30/41	\$ 7,833.44	None	\$ 7,833.44
9/30/42	11,915.67	None	11,915.67
Total	\$19,749.11	None	\$19,749.11
	Declared Value-Excess Tax		
9/30/41	\$ 4,565.41	None	\$ 4,565.41
9/30/42	1,687.10	None	1,687.10
Total	\$ 6,252.51	None	\$ 6,252.51

In making this determination of your tax liability careful consideration has been given to the report of examination dated January 27, 1945.

No deduction is allowed herein for declared value excess profits tax because your net income is determined upon the cash receipts and disbursements basis and no declared value excess-profits tax was paid in either of the taxable years herein.

Adjustments to Net Income

Taxable Year Ended September 30, 1941

Net income (loss) as disclosed by return (\$ 93,811.44)

Unallowable deductions:

(a) Taxes	\$100,623.73	
Forwarded:	\$100,623.73	(\$ 93,811.44)
2—Birch Ranch & Oil Co.		Statement
Brought forward:	\$100,623.73	(\$ 93,811.44)
(b) Interest	2,075.32	
(c) Net operating loss deduction	81,386.64	184,085.69

Total \$ 90,274.25

Reductions in income:

(d) Partnership loss	\$ 32,221.63	
(e) Conaway Ranch income	20,154.64	
(f) Etiwanda Citrus Ranch income	186.70	
(g) Compensation for services	3,000.00	55,563.01

Net income adjusted \$ 34,711.24

## Explanation of Adjustments

(a) The deduction (claimed as taxes) of \$120,000.00 interest on \$2,000,000.00 of bonds issued by Reclamation District No. 2035 is disallowed except as to \$19,200.00 paid to the Hopkins sisters and Miss Minter. The disallowed amount of \$100,800.00 is reduced to \$100,623.73 by allowance of an additional amount of \$176.27 real estate taxes.

(b) Interest on indebtedness incurred or continued to purchase or carry obligations the interest upon which is wholly exempt from tax is disallowed. Section 23(b) of the Internal Revenue Code.

(c) There is no amount of net operating loss deduction allowable for this taxable year under the provisions of section 122 of the Internal Revenue Code.

(d) You failed to claim a deduction for your distributive share of loss of the partnership Birch-Royer Oil Company, for the taxable year ended December 31, 1940, the amount of which has been determined as \$32,221.63.

(e) The following adjustments are made in the computation of Conaway Ranch income:

Decreases:		
1. Closing inventory eliminated		\$69,522.43
2. Depreciation of breeding sheep		5,426.51
	Total	<hr/> \$74,948.94
Forwarded:		\$74,948.94
3—Birch Ranch & Oil Co.		Statement
Brought forward:		<hr/> \$74,948.94
Increases:		
3. Opening inventory eliminated	\$44,660.90	
4. Cost of breeding sheep disallowed	10,133.36	54,794.26
	Net decrease	<hr/> \$20,154.68

1 and 3. Inventories are disregarded because the Conaway Ranch net income is determined upon the cash receipts and disbursements basis.

2 and 4. The cost of breeding sheep purchased in the taxable year is disallowed as representing a capital expenditure, \$10,133.36, and depreciation is allowed on the cost of breeding sheep purchased in prior years and the taxable year in the amount of \$5,426.51.

(f) Income of Etiwanda Citrus Ranch is reduced \$186.70 due to the elimination of closing inventory of fruit produced. The net income of Etiwanda Citrus Ranch is determined upon the cash receipts and disbursements basis.

(g) An additional deduction of \$3,000.00 is allowed for compensation of services rendered by George W. Clemson, this amount having been paid in the taxable year and your net income being determined upon the cash receipts and disbursements basis.

Computation of Declared Value Excess-Profits Tax

Taxable Year Ended September 30, 1941

Net income \$34,711.24

Less: 10% of \$999.00, value of capital stock as declared in your capital stock tax return for the year ended June 30, 1941 99.90

Net income subject to declared value excess-profits tax \$34,611.34  
5% of declared value of capital stock 49.95

Balance \$34,561.39

4—Birch Ranch & Oil Co. Statement

Declared value excess-profits tax:

6 % of \$ 49.95 \$ 3.00  
12 % of \$34,561.39 4,147.37

Total \$4,150.37  
Plus: Defense tax (10% of \$4,150.37) 415.04

Correct declared value excess-profits tax liability \$ 4,565.41

Declared value excess-profits tax assessed:  
Original, account No. 850019 None

Deficiency of declared value excess-profits tax \$ 4,565.41

Computation of Income Tax

Taxable Year Ended September 30, 1941

Net income \$34,711.24

Normal-tax net income \$34,711.24

Income tax:

Tax on \$25,000.00 \$3,775.00  
35 % of \$ 9,711.24 3,398.93

Total \$7,173.93  
Plus: Defense tax (1.9% of \$34,711.24) 659.51

Correct income tax liability \$ 7,833.44

Income tax assessed: Original, account No. 850019 None

Deficiency of income tax \$ 7,833.44

## 5—Birch Ranch &amp; Oil Co.

Statement

Adjustments to Net Income  
Taxable Year Ended September 30, 1942

Net income (loss) as disclosed by return (\$ 53,475.88)

## Unallowable deductions:

(a) Taxes	\$102,423.24	
(b) Interest	1,869.63	
(c) Partnership loss	32,221.63	
(d) Compensation for services	7,200.00	143,714.50

Total		\$ 90,238.62
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## Reductions in income:

(e) Conaway Ranch income	\$ 45,341.54	
(f) Etiwanda Citrus Ranch income	7,116.00	52,457.54

Net income adjusted		\$ 37,781.08
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## Explanation of Adjustments

(a) The deduction (claimed as taxes) of \$120,000.00 interest on \$2,000,000.00 of bonds issued by Reclamation District No. 2035 is disallowed except as to \$18,990.00 paid to the Hopkins sisters and Miss Minter. A further disallowance of \$1,413.24 is made on account of an excessive deduction for real estate taxes.

(b) Interest on indebtedness incurred or continued to purchase or carry obligations the interest upon which is wholly exempt from tax is disallowed. Section 23(b) of the Internal Revenue Code.

(c) The deduction of \$32,221.63 claimed as your distributive share of loss of the partnership Birch-Royer Oil Company for its taxable year ended December 31, 1940, is disallowed. The deduction has been allowed for your taxable year ended September 30, 1941.

(d) The deduction of \$7,200.00 claimed for compensation paid prior to the taxable year for services of George W. Clemson is disallowed because the amount was paid prior to the taxable year and your net income is determined upon the cash receipts and disbursements basis.

(e) The following adjustments are made in the computation of Conaway Ranch income:

## 6—Birch Ranch &amp; Oil Co.

Statement

## Decreases:

1. Closing inventory eliminated	\$110,996.99
2. Depreciation of breeding sheep	3,866.98

Total	\$114,863.94
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## Increase:

3. Opening inventory eliminated	69,522.43
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Net decrease	\$ 45,341.51
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1 and 3. Inventories are disregarded because the Conaway Ranch net income is determined upon the cash receipts and disbursements basis.

2. Depreciation is allowed on the cost of breeding sheep purchased in prior years in the amount of \$3,866.98.

(b) Income of Etiwanda Citrus Ranch is reduced \$7,116.00 due to the elimination of inventories of fruit produced—\$7,302.70 at the close of the year and \$186.70 at the beginning of the year. The net income of Etiwanda Citrus Ranch is determined upon the cash receipts and disbursements basis.

Computation of Declared Value Excess-Profits Tax

Taxable Year Ended September 30, 1942

Net income	\$37,781.08
Less: 10% of \$200,000.00, value of capital stock as declared in your capital stock tax return for the year ended June 30, 1942	20,000.00
Net income subject to declared value excess-profits tax	\$17,781.08
5% of declared value of capital stock	10,000.00
Balance	\$ 7,781.08
Declared value excess-profits tax:	
6.6% of \$10,000.00	\$ 660.00
13.2% of \$ 7,781.08	1,027.10
Correct declared value excess-profits tax liability	\$ 1,687.10
Forwarded:	\$ 1,687.10
7—Birch Ranch & Oil Co.	Statement
Brought forward:	\$ 1,687.10
Declared value excess-profits tax assessed:	
Original, account No. 10467	None
Deficiency of declared value excess-profits tax	\$ 1,687.10



Computation of Income Tax  
Taxable Year Ended September 30, 1942

## Tentative tax under section 108(a)(1)(A), I. R. C.

1. Net income			\$37,781.08
2. Normal-tax net income			\$37,781.08
3. Surtax net income			\$37,781.08
4. Income tax:			
Normal tax:			
Tax on \$25,000.00	\$4,250.00		
37% of \$12,781.08	4,729.00	\$	8,979.00
Surtax:			
Tax on \$25,000.00	\$1,500.00		
7% of \$12,781.08	894.68		2,394.68
5. Tentative tax			\$11,373.68

## Tentative tax under section 108(a)(1)(B), I. R. C.

6. Net income			\$37,781.08
7. Normal-tax net income			\$37,781.08
8. Surtax net income			\$37,781.08
9. Income tax:			
Normal tax:			
Tax on \$25,000.00	\$4,250.00		
31% of \$12,781.08	3,962.13	\$	8,212.13
Surtax:			
Tax on \$25,000.00	\$2,500.00		
22% of \$12,781.08	2,811.84		5,311.84
10. Tentative tax under section 108(a)(1)(B)			\$13,523.97
8—Birch Ranch & Oil Co.			Statement
Income tax under section 108(a)(1), I. R. C.			
11. Number of days in taxable year			365
12. Number of days before July 1, 1942			273
13. Number of days after June 30, 1942			92
14. Portion of item 5 which item 12 bears to item 11 ( $\$11,373.68 \times 273/365$ )		\$	8,506.89
15. Portion of item 10 which item 13 bears to item 11 ( $\$13,523.97 \times 92/365$ )			3,408.78
16. Correct income tax liability			\$11,915.67
17. Income tax assessed: Original, account No. 10467			None
18. Deficiency of income tax			\$11,915.67

Received and filed T. C. U. S. July 13, 1945.

[Title of Tax Court and Cause.]

## AMENDED PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiencies set forth by the Commissioner of Internal Revenue in Notice of Deficiency and Statement, L. A.: T.: 90:P. B., dated April 30, 1945, and alleges as follows:

I. Petitioner is a corporation organized and existing under the laws of the State of Nevada with its principle office at 427 West Fifth Street, Los Angeles, California. The returns for the periods here involved were filed with the Collector of Internal Revenue for the Southern District of California at Los Angeles, California.

II. The said Notice of Deficiency and Statement, a copy of which is hereto attached marked "Exhibit A," was mailed to the petitioner on April 30, 1945.

III. The taxes in controversy are income and excess profit taxes for the fiscal years ending September 30, 1941, and September 30, 1942, and involve amounts as follows:

Year Ended	Liability	Assessed	Deficiency
Income Tax			
9/30/41	\$ 7,833.44	None	\$ 7,833.44
9/30/42	11,915.67	None	11,915.67
Total	\$19,749.11	None	\$19,749.11
Declared Value Excess-Profits Tax			
9/30/41	\$ 4,565.41	None	\$ 4,565.41
9/30/42	1,687.10	None	1,687.10
Total	\$ 6,252.51	None	\$ 6,252.51

The entire deficiency is in controversy for each of said years. Also, as hereinafter shown, petitioner is entitled to credits which would in any event offset the whole of such deficiency for each of said years.

IV. The determination of the taxes set forth in said notice of deficiency is based upon the following errors of the Commissioner:

(a) In holding that the petitioner's net income for both of said fiscal years is determined upon the cash receipts and disbursements basis, when in fact the petitioner's net income, since its organization on October 15, 1934, at all times has been and is determined upon an accrual basis of accounting.

(b) In disregarding the inventories covering petitioner's Conaway Ranch for each of said fiscal years upon the theory that the net income of said ranch is determined upon the cash receipts and disbursements basis, when in fact the net income of said ranch, and petitioner's entire system of accounting, at all times has been and is determined upon an accrual basis.

(c) In holding that the income of petitioner's Etiwanda Citrus Ranch, and its system of accounting, for each of said fiscal years is upon the cash receipts and disbursements basis, when in fact the net income of said ranch, and petitioner's entire system of accounting, at all times has been and is determined upon an accrual basis.

(d) In disallowing petitioner's deduction for the year ending September 30, 1941, in the sum of

\$120,000.00, except as to \$19,200.00 thereof, upon the theory that the same represents interest, when in fact the whole of such item of deduction represents, and is properly deductible as, taxes accrued to pay interest on \$2,000,000.00 of bonds issued by Reclamation District No. 2035, the principal of all of which bonds, with interest thereon, until paid constitutes a lien against petitioner's lands, and which interest accrues semi-annually as a lien and tax against petitioner's lands irrespective of the occurrence of any other event.

(e) In disallowing petitioner's deduction for the year ending September 30, 1942, in the sum of \$120,000.00, except as to \$19,200.00 thereof, upon the theory that the same represents interest, when in fact the whole of such item of deduction represents, and is properly deductible as, taxes accrued to pay interest on \$2,000,000.00 of bonds issued by Reclamation District No. 2035, which interest accrues semi-annually as a lien and tax against petitioner's lands irrespective of the occurrence of any other event.

(f) In disallowing petitioner's net operating losses deducted by it in its income tax returns for the said taxable years ending September 30, 1941 and 1942, under the theory that such losses are not deductible under the provisions of Section 122 of the Internal Revenue Code.

(g) In disallowing the petitioner's deductions in its said income tax returns for each of said years for declared value excess profits for the erroneous reason that petitioner's net income is determined



upon the cash receipts and disbursements basis when in fact, such net income is determined upon an accrual basis.

V. The facts upon which the petitioner relies as a basis for this proceeding are as follows:

(a) Petitioner was organized as a corporation on October 15, 1934; that at the time of its organization, petitioner adopted a fiscal year commencing on October 1 and ending on September 30, and a system of accounting upon an accrual basis; that petitioner has not since changed said fiscal year or its said system of accounting: that ever since said date of organization the petitioner has entered upon its books of account all accounts receivable and accounts payable when and as the same accrued and petitioner has determined its net income and made its income tax returns upon said accrual basis of accounting. That the Commissioner has nevertheless disallowed the various items as set forth in said deficiency notice and statement (hereto attached as Exhibit "A"), and as hereinafter referred to, upon the erroneous theory that petitioner's system of accounting is upon a cash basis.

(b) Ever since its said date of organization petitioner has owned and operated a ranch known as the Conaway Ranch; that all transactions concerning the operation of said ranch have been entered in a separate set of books; that at the time of petitioner's organization it adopted an accrual system of accounting for the said ranch and petitioner has not since changed its said system of accounting; that ever since said date petitioner has entered upon its



books of account concerning said ranch all accounts receivable and all accounts payable when and as the same accrued and the petitioner has determined its net income from said ranch and all of its net income upon said accrual basis of accounting. That the Commissioner has nevertheless disallowed the various items relating to said Conaway Ranch as set forth in said deficiency notice and statement (hereto attached as Exhibit "A") upon the theory that this petitioner's system of accounting with relation to said ranch is upon a cash basis.

(c) Ever since its said date of organization petitioner has owned and operated what is known as the Etiwanda Citrus Ranch; that at the time of petitioner's organization it adopted an accrual system of accounting for the said ranch and petitioner has not since changed its said system of accounting; that ever since said date petitioner has entered upon its books of account concerning said ranch all accounts receivable and all accounts payable when and as the same accrued and the petitioner has determined its net income from said ranch and all of its net income upon said accrual basis of accounting; that the Commissioner has nevertheless treated this petitioner's system of accounting as if said system with relation to said ranch were upon a cash basis.

(d)1. Ever since prior to the year 1872 it has been the policy of the State of California to encourage the development of marginal and undeveloped swamp and overflowed lands by providing for the formation of reclamation districts, constitut-

ing municipal corporations as separate legal entities, and by providing for the financing of such districts by the issuance of reclamation bonds with liberal payment and tax exemption privileges, and other privileges, and by providing that the principal and interest of such bonds shall constitute a first and prior lien until paid upon all of the lands of such districts.

2. In reliance upon the said policy and the laws of said State for the encouragement of the development of said marginal lands, the petitioner's predecessors in interest in the ownership of the said Conaway Ranch and other owners of land in the vicinity thereof, on or about April 8, 1919, caused to be created and said lands to be included in Reclamation District No. 2035 of the State of California; that said reclamation district consists of approximately 22,000 acres located in Yolo County, California, and it ever since has been and now is a bona fide duly organized and existing reclamation district of said State.

3. At the said time of said organization of said district the landowners of said district transferred by deed to said district, rights of way and lands for roads, levees, ditches, pumping plants and warehouses, hereinafter referred to as said property; that said district as a separate entity ever since has been and now is the owner of said property.

4. Commencing immediately after the formation of said district the said district caused said property to be improved by the construction of approxi-

mately forty-five miles of roadways, forty-seven miles of irrigation canals, fifty-five miles of drainage canals and ditches, together with bridges, pumping plants, warehouses and other structures usual and necessary for the development and operation of such a district; that said improvements were completed prior to 1925 at a cost slightly in excess of the sum of \$2,000,000.00.

5. In order to pay for the cost of said improvements and pursuant to the provisions of Section 3457 of the Political Code of the State of California, the said district duly caused to be issued a bond issue in the sum of \$2,000,000.00 covering all of the lands of said district; that said bonds are each dated January 21, 1925, and each bear interest at the rate of 6% per annum, payable on the 1st day of January and the 1st day of July of each and every year until paid, and said bonds mature each year in series commencing on the 1st day of January, 1935, up to and including January 1st, 1943; that under the laws of said State the said interest accrues in the manner aforesaid and becomes a tax lien against the petitioner's land irrespective of any act of said Reclamation District or of any call by the County Treasurer, and said interest remains a tax lien upon the whole of petitioner said Conaway Ranch until paid.

6. Between 1925 and 1934 two of petitioner's predecessors in interest, to wit: A. Otis Birch and wife, acquired the title to the whole of the said Conaway Ranch and they also acquired all of the other

parcels of land comprising said district, except one small parcel, and caused such additional parcels so acquired to be and become a part of said Conaway Ranch; that between said dates said Birch and wife also acquired the ownership of a large majority of said bonds; that ever since 1934 except for said one parcel of land, and except for said property of said district, said Conaway Ranch has comprised the entire area of said district.

7. With respect to their income tax returns for each year between 1925 and 1934 said Birch and wife adopted the practice of deducting, and they did deduct, said item of \$120,000.00 as taxes, the same representing an amount sufficient to pay the total annual interest accruing upon said \$2,000,000.00 of bonds; also in said income tax returns for each of said years said Birch and wife did not account for or include as part of their gross income, any part of the interest received by them from any of said bonds upon the theory that such income was exempt from taxation under the laws of the State of California.

8. The Commissioner questioned each of said deductions for each of said years and said failure to include said income from said bonds, and in each instance, after investigation and consideration the Commissioner approved each of said deductions and said failure to include said income.

9. Ever since the said development of said district said Conaway Ranch has been operated as a farm in the raising of rice and sheep and other



farm products. Such operations require current financing in a sum substantially in excess of \$100,000.00 per year. After the commencement of the depression in 1929, A. Otis Birch and wife found it inconvenient to advance such current financing and they found it necessary and desirable to borrow money for such purpose. On attempting so to do, they found it then was the policy of all financial institutions not to loan such sums of money to individual persons and that it was impossible for them to borrow any substantial sum from such institutions, or at all, unless they should place a substantial part of their property in a corporate form of ownership.

10. Solely for the purpose of obtaining said current financing, and other financing, and for the purpose of enjoying the legitimate advantages of a corporate form of organization, said Birch and wife caused the petitioner herein to be incorporated on the 15th day of October, 1934, in the State of Nevada. On the same date and for the same reasons and as part of a convenient corporate set-up for the proper segregation of their properties, they also caused to be incorporated the Birch Securities Company, a corporation of the State of Nevada, and the Birch Holding Company, a corporation of the State of Delaware. Said Birch and wife thereupon transferred all of the aforesaid bonds owned by them to said Birch Securities Company and the whole of said Conaway Ranch, together with a portion of all other properties owned by them, to the petitioner herein. The petitioner and said Birch Securities



Company thereupon issued all of their respective authorized capital stock and transferred the same to the Birch Holding Company and said Birch Holding Company thereupon issued all of its capital stock and transferred 49% thereof to A. Otis Birch and 51% thereof to M. Estelle C. Birch, his wife, each of which persons owned all of said capital stock during the fiscal years involved herein.

11. The organization of all of said companies was made in good faith and was bona fide in every respect and said organization was not made with a view to affecting in any manner the obligation of said Birch and wife, or of any of said companies, to pay taxes of any kind or character, nor was it made for the purpose of enabling petitioner to take the deductions involved herein for taxes paid to said reclamation district, since the said Birch and wife for approximately eight years prior to the organization of said companies had been after full consideration by the Commissioner, as aforesaid, permitted to take said deductions from their income tax returns for each of said years.

12. Since its incorporation the petitioner has borrowed various sums of money from various banks and other financial institutions to the extent of substantially in excess of \$100,000.00 a year. The petitioner has ever since its organization engaged in the business of operating said ranch and of developing oil wells and other enterprises as a separate legal entity separate and apart from the activities and obligations of said Birch and wife and of said

other companies. Ever since its organization petitioner has had its separate creditors, separate and apart from said Birch and wife and said other companies, and said financial institutions and various other creditors have extended credit to the petitioner in reliance upon the fact that the petitioner is a separate corporate entity which is responsible for the payment of no obligations, including taxes, other than its own.

13. Petitioner is in fact a separate legal and corporate entity and it is not in any respect the alter ego of said Birch and wife or of said other corporations, or any of them, or of any other person or corporation, and its organization, and the aforesaid set-up, are legitimate and bona fide in every respect.

14. On October 15, 1934, the ownership of said bond issue was as follows:

Republic Life Insurance Company	\$ 86,000.00
Lula M. Minter	10,000.00
The Hopkins	309,000.00
A. Otis Birch and wife	1,595,000.00
<hr/>	
Total	\$2,000,000.00

15. That during 1941 and 1942 the ownership of said bonds was as aforesaid except that the Birch Securities Company on October 15, 1934, acquired the aforesaid bonds owned by A. Otis Birch and wife, of the said face value of \$1,595,000.00, and except that in 1940 this petitioner acquired said bonds owned by said Republic Life Insurance Company

of the face value of \$86,000.00; that except as aforesaid, this petitioner has not owned, and does not now own, any of said bonds.

16. On October 6, 1934, an election was duly held in said Reclamation District No. 2035 for the refunding of all said bonds, pursuant to the provisions of said Section 3480. At said election the issuance of 2,000 new bonds in the place of said old bonds was duly authorized. Said new bonds mature as stated in said Notice of Election and they are in like number and amount as said old bonds and they likewise bear interest at 6% to the end that such new bonds when issued take the place of said old bonds and to the end that interest upon the entire principal of said bond issue is continuous and a first and prior lien against all of the lands of the said district until said bonds are paid.

17. On or about 1942 said new bond issue was issued in the place of said old bonds. Pursuant to the provisions of said Section 3480 the said lands are subject to a lien of continuously accumulating interest at said rate of 6%, whether said interest accrues from said old bonds or said new bonds, and until said sum of \$2,000,000.00 is paid that all of said bonds are outstanding and unpaid.

18. Since 1925 the petitioner and its said predecessors in interest, in exchange for the use of said property of said district, including said warehouses, has paid all expenses for the operation of said district, so that the only expense which said district has and for which it need raise any taxes is the pay-

ment of said interest on said bonds in the sum of \$120,000.00 per year. By reason of these facts the amount of said Reclamation District tax against petitioner's land is exactly said sum of \$120,000.00 a year, which sum accrues solely by reason of the existence of said bonds and irrespective of the occurrence of any other event.

19. That at all times since its said organization petitioner has paid in cash to the County Treasurer of said Yolo County, or to the bondholders of said bond issue in exchange for an equivalent amount of interest coupons of said bonds, an amount of money or interest coupons sufficient to pay the taxes to meet the interest upon all of said bonds promptly as such interest became due, except that from 1936, up to and including the year 1940, this petitioner did not pay the amount of money necessary to meet the interest coupons as the same accrued upon the aforesaid bonds owned and held by said Birch Securities Company; that petitioner did not make said payments for the reason, among others, that in 1937 the Birch Securities Company became, and ever since has been, suspended by the Franchise Tax Commissioner of the State of California for alleged non-payment of certain California State Franchise taxes; that under the laws of the State of California, the said Birch Securities Company, during the existence of said suspension until 1941, was prohibited from delivering any of the interest coupons of said bonds owned by it, or from accepting any money therefor under penalty of a criminal prosecu-



tion, a severe fine, and possible imprisonment of its officers; that on June 9, 1941, said Birch Securities Company, through its president, A. Otis Birch, in an action entitled, A. Otis Birch vs. Charles J. McColgan, as Franchise Tax Commissioner of the State of California, the same being cause No. 1430B of the District Court of the United States for the Southern District of California, received an opinion from said court, sitting as a three-judge statutory court, to the effect that said suspension of Birch Securities Company was wrongful and void (39 Fed. Supp. 358); that thereafter a permanent injunction was issued by said three-judge statutory court prohibiting said Franchise Tax Commissioner from maintaining said suspension; that thereafter other obstacles which had prevented this petitioner from obtaining said coupons from said Birch Securities Company also became removed, and thereafter, to wit: commencing prior to October 1, 1941, and including the whole of the said fiscal years involved herein, this petitioner commenced to pay money sufficient to meet the interest on all of said bonds, including the said bonds of the said Birch Securities Company, that in every instance where this petitioner has paid money directly to said bondholders in exchange for interest coupons of said bonds, this petitioner has deposited said interest coupons with the County Treasurer of said county as the equivalent of money for the payment of said taxes; that the laws of the State of California permit and expressly provide that the taxes of a reclamation district may be paid in such manner.



20. Upon its books of account, petitioner included, for its fiscal year ending September 30, 1941, items of interest payable and paid on said bonds as taxes to said district in the sum of \$120,000.00. In its income tax return for said year, petitioner deducted said sum of \$120,000.00 as taxes accrued. Said deduction is a proper item of deduction for said purpose. Notwithstanding the facts aforesaid, the Commissioner erroneously disallowed said item in said Notice of Deficiency and Statement.

(e)1. Petitioner hereby incorporates paragraphs (d)1 to (d)20 hereof as part of this paragraph.

2. Upon its books of account, petitioner included for the fiscal year ending September 30, 1942, items of interest payable and paid on said bonds as taxes to said district in the sum of \$120,000.00. In its income tax return for said year, petitioner deducted said sum of \$120,000.00 as taxes accrued. Said deduction is a proper item of deduction for said purpose. Notwithstanding the facts aforesaid, the Commissioner erroneously disallowed said item in said Notice of Deficiency and Statement.

(f)1. Petitioner hereby incorporates paragraphs (d)1 to (d)20 hereof as part of this paragraph.

2. That in its income tax returns for the years ending September 30, 1941 and 1942, the petitioner deducted operating losses in the sums of \$184,085.69 and \$143,714.15, respectively, as shown by the Commissioner's said Notice of Deficiency and Statement; that said operating losses, and each and every

item thereof, were actual operating losses and proper items of deduction; that notwithstanding the facts aforesaid the Commissioner disallowed all of said operating losses upon the erroneous theory that petitioner's net income is determined upon the cash receipts and disbursements basis when in fact said net income should have been and is determined upon said accrual basis.

(g)1. Petitioner hereby incorporates paragraphs (d)1 and (d)20 hereof as part of this paragraph.

2. That by reason of the facts aforesaid, in its said income tax returns for the years ending September 30, 1941 and 1942, the petitioner made no declared value of excess profit tax assessed; that notwithstanding the facts aforesaid the Commissioner in said Notice of Deficiency and Statement erroneously assessed against this petitioner a deficiency of declared value excess profit taxes in the sums of \$4,565.41 and \$1,687.10, respectively, upon the erroneous theory that petitioner's net income is determined upon the cash receipts and disbursements basis when in fact said net income should have been and is determined upon said accrual basis.

(h) That during petitioners fiscal year ending September 30, 1943, petitioner suffered a loss by reason of non-payment of a loan made by it to the Birch-Smith Storage Company, a California corporation, operated and owned independently of said A. Otis Birch and wife, in the sum of \$52,031.26; that during said year petitioner also suffered a loss

of a loan made to one Edna Tiller in the sum of \$200.00; that during said year petitioner also suffered a loss by reason of an unpaid loan made to Mrs. A. E. Dye; that in its income tax return for said year, petitioner listed and deducted said items of loss in the total sum of \$52,481.26; that should this court deny any part of this petitioner's petition herein, this petitioner desires to carry back to its fiscal years ending September 30, 1941 and 1942, as much of said sum of \$52,481.26, up to \$12,000.00 thereof, as may be necessary to offset any part of the said tax deficiencies involved herein.

(i) That during petitioner's fiscal year ending September 30, 1944, petitioner suffered a loss in the sum of \$73,556.88 by reason of the drilling and abandonment of an oil well known as the Stovall-Wilcoxsen well, and the leasehold interest in connection therewith; that in the same year this petitioner suffered losses from sales of property other than capital assets as follows:

A 338-acre farm situated in Stanislaus

County, California .....	\$36,417.50
Lots 61, 112, 141, Tract 993.....	1,160.00
Lots 32, 36, 60, 91, Tract 993.....	1,520.00
Lots 87, 62, 189, 90, 108, Tract 993.....	1,730.00
Lot 201, Tract 993.....	1,200.00
Store Building, 320 Venice Blvd., Los Angeles .....	5,500.00

that in its income tax return for said year petitioner listed and deducted all of the aforesaid items of loss in the total sum of \$121,084.38: that should this

court deny any part of this petitioner's petition herein this petitioner desires to carry back to its fiscal year ending September 30, 1942, as much of said losses in the said sum of \$121,084.38, up to \$25,000.00 thereof, as may be necessary to offset any part of the said tax deficiencies involved herein.

Wherefore, petitioner prays that this court hear this proceeding and that the petitioner be granted relief as follows:

(a) That this court adjudge and declare that this petitioner's net income, and its system of accounting, for said fiscal years ending September 30, 1941 and 1942, and for all years, has been and is determined upon an accrual basis.

(b) That this court adjudge and declare that this petitioner's net income, and its system of accounting relating to said Conaway Ranch for each of said years, and for all years, is determined upon an accrual basis.

(c) That this court adjudge and declare that this petitioner's net income, and its system of accounting, relating to said Etiwanda Citrus Ranch, for each of said years, and for all years, is determined upon an accrual basis.

(d) That this court determine that the petitioner is entitled to a deduction in the full sum of \$120,000.00, accrued as taxes for payment of interest upon bonds of Reclamation District 2035 of the State of California for the fiscal year ending September 30, 1941.

(e) That this court determine that the petitioner



is entitled to a deduction in the full sum of \$120,000.00, accrued as taxes for payment of interest upon bonds of Reclamation District 2035 of the State of California for the fiscal year ending September 30, 1942.

(f) That this court determine that this petitioner is entitled to deduct the operating losses as deducted by it in its income tax returns for the said taxable years ending September 30, 1941 and 1942, and as disallowed by the Commissioner in said Notice of Deficiency and Statement.

(g) That this court determine that this petitioner's failure to include in its said income tax returns for each of said years any declared value excess profits is proper, and that the Commissioner's assessed deficiencies therefor, are erroneous and improper.

(h) That should this court deny any part of this petitioner's petition herein that petitioner be adjudged entitled to carry back to its fiscal years ending September 30, 1941 and 1942, as much of said sum of \$52,481.26, up to \$12,000.00 thereof, as may be necessary to offset any part of the said tax deficiencies involved herein.

(i) That should this court deny any part of this petitioner's petition herein that petitioner be adjudged entitled to carry back to its fiscal year ending September 30, 1942, as much of said losses in the said sum of \$121,084.38, up to \$25,000.00 thereof, as may be necessary to offset any part of the said deficiencies involved herein.

(j) That this court disallow and redetermine all



of the said deficiencies as determined by the Commissioner in said Notice of Deficiency and Statement.

GEORGE ACRET,

/s/ GEORGE ACRET,

Attorney for Petitioner.

State of California,

County of Los Angeles—ss.

R. R. Landrum, being duly sworn, says that he is the Secretary of the petitioner and that he is duly authorized to verify the foregoing petition in behalf of the petitioner; that he has read the foregoing petition and is familiar with the statements contained therein and that all of the statements contained therein are true except those stated to be upon information and belief, and all of such statements he believes to be true.

R. R. LANDRUM,

/s/ R. R. LANDRUM.

Subscribed and sworn to before me this 20th day of July, 1945.

[Seal] /s/ WILLIAM R. LAW,

Notary Public in and for the County of Los Angeles, State of California.

Received and Filed T.C.U.S., July 25, 1945.

[Title of Tax Court and Cause.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the amended petition of the above-named taxpayer, admits and denies as follows:

I and II. Admits the allegations contained in paragraphs I and II of the amended petition.

III. Admits that the taxes in controversy are income and declared value excess-profits taxes for the fiscal years ending September 30, 1941, and September 30, 1942, as alleged in paragraph III of the amended petition and denies the remaining allegations contained in said paragraph.

IV (a) to (g), inclusive. Denies the allegations of error contained in subparagraphs (a) to (g), inclusive, of paragraph IV of the amended petition.

V (a), (b) and (c). Denies the allegations contained in subparagraphs (a), (b), and (c) of paragraph V of the amended petition.

(d) 1 to (d) 19, inclusive. Denies the allegations contained in subparagraphs (d) 1 to (d) 19, inclusive, of paragraph V of the amended petition.

(d) 20. Admits that in its income tax return for its fiscal year ending September 30, 1941, petitioner deducted said sum of \$120,000.00 as taxes accrued as alleged in subparagraph (d) 20 of paragraph V of

the amended petition and denies the remaining allegations contained in said subparagraph.

(e) 1. Denies the allegations contained in subparagraph (e) 1 of paragraph V of the amended petition.

(e) 2. Admits that in its income tax return for the fiscal year ending September 30, 1942, petitioner deducted said sum of \$120,000.00 as taxes accrued as alleged in subparagraph (e) 2 of paragraph V of the amended petition and denies the remaining allegations contained in said subparagraph.

(f) 1 and (f) 2. Denies the allegations contained in subparagraphs (f) 1 and (f) 2 of paragraph V of the amended petition.

(g) 1 and (g) 2. Denies the allegations contained in subparagraphs (g) 1 and (g) 2 of paragraph V of the amended petition.

(h) and (i). Denies the allegations contained in subparagraphs (h) and (i) of paragraph V of the amended petition.

VI. Denies generally and specifically each and every allegation contained in the amended petition not hereinbefore expressly admitted, qualified or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ J. P. WENCHEL,  
Chief Counsel, Bureau of  
Internal Revenue.

ECC

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

E. C. CROUTER,

H. A. MELVILLE,  
Special Attorneys,  
Bureau of Internal Revenue.

Received and Filed T. C. U. S. August 29, 1945.

The Tax Court of the United States

Docket No. 8720

BIRCH RANCH &amp; OIL COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

June 30, 1947—10:10 A.M.

(Met pursuant to notice.)

Before: Honorable John W. Kern,  
Judge.

Appearances:

GEORGE H. ACRET,

650 South Grand Avenue,  
Los Angeles, California,

Appearing for the Petitioner.

EARL C. CROUTER,

(Honorable J. P. Wenchel, Chief Counsel,  
Bureau of Internal Revenue),

Appearing for the Respondent.

## PROCEEDINGS

The Court: I will call Docket 8720.

Mr. Acret: Ready for the Petitioner. George  
Acret.



Mr. Crouter: Respondent is ready, if the Court please. Earl C. Crouter for the Respondent.

Mr. Acret: I have a plan of procedure here, your Honor, which I think should shorten this matter down to less than 10 minutes, plus the time necessary to make an opening statement. I think an opening statement acquainting your Honor with the history of this matter and the facts, as found in a form of proceeding, will shorten this down.

I presume your Honor would like to save the time at this time if it is possible to do.

The Court: Your supposition is correct. May I have a statement as to the issues?

Mr. Acret: Yes, your Honor. The issues concern a deficiency—by the way, may I ask if your Honor has read the amended petition? We had one printed that contains a complete statement of the ultimate facts and the facts are complicated and they're in considerable detail. I think it is a 21-page printed petition.

The Court: Yes, I see it.

Mr. Acret: Your Honor has not had time to read it?

The Court: I have not read it. [3\*]

## OPENING STATEMENT ON BEHALF OF THE PETITIONER

By Mr. Acret:

The deficiency concerns the years ending September 30, 1941, and September 30, 1942. The Petitioner,

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\* Page numbering stamped at top of page of original Reporter's Transcript.

the corporation has its system of accounting on a basis of fiscal year ending September 30th. The main point that has been previously in litigation, concerning the same right to a deduction, which is involved here and which is a deduction made by the Petitioner of \$120,000.00, paid by it to meet taxes which accrue as a matter of law, to meet 6 per cent interest on \$2,000,000.00 bond issue of reclamation bonds which are against Petitioner's lands.

The facts and the history and the findings of fact in a former case concerning the Petitioner's right to make this same deduction for the year, I think it was 1937, 1939, are contained in Docket No. 109993, in which Judge Turner made findings of fact under date of April 20, 1944.

The Court: That was a memorandum of finding of facts.

Mr. Acet: That was a memorandum of finding, yes, sir, your Honor, findings in the case.

The material facts which ought to be stated to the Court at this time are as follows: As will appear the laws of the State of California commencing way back in 1880 held out to persons undertaking to reclaim waste lands in [4] California the inducement that there might be a bond issue on the money spent, a reclamation district formed and a bond issue covering the money spent in improving the reclamation district, and that the interest on such bonds would be exempt interest.

Commencing about 1918, in order to take advantage of this inducement that was held out A. Otis Birch and a group associated with him acquired

about 20,000 acres of these waste lands in the Sacramento Valley in Yolo County, about 14 miles out of Sacramento.

They proposed a plan for improvement of the district and petitioned for the formation of a district within a certain area under the law relating to reclamation districts in California. They proposed that some 18 parcels of land, in addition to their own parcel, including about 20,000 acres, making a total of about 22,000 acres be included in the district.

Some of the parcels were rejected at a vote held for the purpose of forming the district, or rather by the board of supervisors of the county, as provided by law, and other additional parcels were brought in. The district was formed in 1918, including approximately 13 separate parcels of land, of which the parcel involved herein was one.

Mr. A. Otis Birch and his associates undertook to make improvements of the district in accordance with the [5] plan which was adopted and approved by the supervisors of the district, and approved by the State Engineer for the reclamation district.

Whatever money Mr. Birch and his associates spent—the exact amount is immaterial—it is sufficient they built some 45 miles of road and 47 miles of canals, for which the members of the district approved their right to receive a warrant in the sum of \$2,000,000.00. That warrant being unpaid, that is, still in 1918, in accordance with the forms of law, a \$2,000,000.00 bond issue was duly voted to pay this \$2,000,000.00 warrant and the bonds in exchange for the warrant were turned over to Birch and his as-

sociates. During this period when they were turning in the warrants and completing the work Mr. Birch and his associates acquired all of the parcels of land in the district. Subsequently Mr. Birch and his wife acquired, from time to time, additional bonds and they bought out the interest of Mr. Birch's associates in the land itself; the Conaway ranch then consisting of 22,000 acres.

On each year after the bonds became due, which according to my recollection, after they became in force, was some years after 1918; and in any event before 1925 Mr. Birch and wife themselves paid into the district the sum of \$120,000.00, to enable the district to meet the interest on these bonds, and which were then owned by themselves. [6]

Under the statute these bonds, including their interest at 6 per cent a year, and which becomes due on July 1st and January 1st, \$60,000.00 each paying date, these bonds by statute become a lien on the land until paid. That is, including interest and principal.

It happens there was—I mention this—a refunding of these bonds, authorized in 1935. The bonds run 10 years, but due to the fact that some of Mr. Birch's associates still owned the bonds and they wouldn't turn them in, the actual refunding could never be accomplished and it never was accomplished until after the tax, the years involved in this tax assessment. As a matter of fact, I understand it wasn't accomplished until 1946, at which time there was a third bond issue. I will state to your Honor at this time there is nothing involved here for the



future, because Mr. Birch and wife no longer own the bonds, and they no longer own the ranch; they sold the bonds.

This whole venture was very unfortunate and expensive in that the ranch never paid Mr. and Mrs. Birch any yield at all on the amount of their investment, which was in excess of \$2,000,000.00. In fact, there were continuous losses.

Mr. and Mrs. Birch deducted this \$120,000.00, which they paid to the County Treasurer to enable the district to meet this interest on these bonds each year, [7] in making tax returns, and as found by Judge Turner the Commissioner questioned the propriety of their doing this, and after an audit was made and an investigation made of the situation in each instance their right to make this deduction was approved by the Commissioner.

The facts would appear that when Mr. Birch took over the entire ranch of 22,000 acres he made a deal with the district and which, frankly, was with the board of directors of the district, persons, of course, elected by himself. They were, nevertheless, legitimate and actual directors and the district is independent, an independent state agency, created by statute.

Mr. Birch and wife deeded to the district land sufficient to enable the district to have its own roads and the right-of-way through all the ditches and two acres for a warehouse belonging to the district. They made a deal with the district whereby, if they maintained this land and these rights-of-way and the ditches, that they would have no expense from the

district, other than the expense to meet these bonds. So that the amount of the expense of the district and the amount of the district's tax was in the sum of \$120,000.00 a year, a fixed sum, irrespective of the occurrence of any other events. That accrued by statute and was an accumulating lien on Petitioner's land, and irrespective of whether or not the [8] County Treasurer made any call or any assessment on these bonds. The interest accumulated as a lien just by statute.

In 1934 Mr. Birch was then nearing 70 years of age and the banks required of him, before he could have any further financing, to put his property in a corporate form. At that time the Birch Ranch & Oil Company, together with other corporations which are immaterial here, for reasons that should appear from the facts, were formed.

Judge Turner found that the corporation was formed to enable the Conaway Ranch to get, or Mr. Birch to get bank credit, a legitimate reason for forming the corporation. The corporation, it would appear, was not formed for any purpose to avoid taxes, because Mr. Birch was being permitted to make the deduction of \$120,000.00 a year, when he owned both the land and the bonds, and just because he formed the corporation seems to have clouded the issues here. It should increase the right to deduct and not decrease it. In any event, the right to make the deduction existed all the time.

After its formation as a corporation in 1934 the corporation purported to place its system of accounting on an accruable basis. It had varied operations,

including the operation of certain oil wells, several ranches down here in Southern California and the Conaway Ranch in Yolo County. [9]

Mr. and Mrs. Birch, in forming the corporation, did not transfer all of their property to the corporation but held out in their own individual names property of the value of about \$600,000.00. So it would seem there could be no question of alter ego.

The corporation in 1934, it being in the midst of the depression, was not able to make the payments to the County Treasurer of \$120,000.00, and it accrued that amount as taxes on its books. As a matter of fact, it was not able to make any substantial payment to the County Treasurer at the time of the trial, up to and including the time of the trial before Judge Turner, and it did not make substantial payments until commencing about 1944 when the financial situation was different than it had been at the time the corporation was first formed.

The Commissioner assessed a deficiency for 1937 and 1939, I think the years were, which was the reason of the Petitioner's deduction of that \$120,000.00 as taxes on an accruable basis; and that is the Petitioner's right to do. That is the matter which was heard before Judge Turner.

Judge Turner made a complete findings of fact which are very efficient and able, and which is the correct statement of the facts, I think, in every respect. This matter was heard for about four days. The only question that we think went off was that Judge Turner concluded [10] from the facts that the amount paid by the taxpayer to meet the interest on

the bonds was the payment of interest, and stated that is the only misstatement of facts, that the taxpayer accrued the payment of interest paid. It was accrued as taxes paid and it was deducted in its income tax return as taxes paid.

It would appear that is the proper way to do it, by virtue of the Little case, which involved a similar situation, in Idaho, concerning irrigation bonds, in which this Court pointed out that the land owner and the owner of the bonds, and the district were three different entities, and what the landowner paid was the taxes to allow the district to meet the interest on the bonds. It would appear that, to be correct, that was a situation where the Commissioner so concerned—the landowner deducted it as interest. The Court held it couldn't be deducted as interest, but should be deducted as taxes.

The Court: What is the difference, Mr. Acret?

Mr. Acret: It will make no difference here, except it did with Judge Turner because—I can't quote offhand the section of the code, but the amount that we paid wasn't within the period that the taxable year, within two months thereof; that made the difference in that case.

The Court: Yes. [11]

Mr. Acret: It doesn't make any difference here, for reasons which I am about to state.

Your Honor may be wondering why we started this action, when this proceeding—on the basis of my statement concerning Judge Turner's findings of fact. Judge Turner's findings of fact, he allowed the interest which the Petitioner paid to the district to



meet the interest for certain bonds owned by third parties. The Commissioner hadn't allowed those, and Judge Turner made findings of fact, ultimate facts, from which it appears it is a necessary conclusion of law the bonds are bona fide and the organization of the district is bona fide and the organization of the corporation is bona fide, and he allowed the deductions which the corporation actually paid for the year in question, and disallowed other deductions because he held as to the ranch books we were not on an accruable basis and on a cash basis.

Now, here comes the crux of the situation with reference to this case. We appealed from that decision, or we petitioned for a right of certiorari to the Supreme Court, questioning the finding that we were not on an accruable basis. The Supreme Court denied our petition and it is my belief that the Government in this former case is *res judicata*. It is also my belief that Judge Turner's findings of fact concerning almost identical [12] transactions and identical deductions are the facts of the case, as far as, even as this case is concerned.

The Court: Who was the taxpayer in that case?

Mr. Acret: The Birch Ranch & Oil Company.

The Court: Oh.

Mr. Acret: What has happened since, your Honor, since we filed the petition, we were not only denied the petition for a writ of certiorari but in auditing the Petitioner's books for 1944 the Commissioner of Internal Revenue has fixed and determined a per cent to that, the fact that Petitioner is on a cash basis. One of the things we wanted to

know is whether we are on an accruable basis or whether we are on a cash basis. That seems to have been fixed by the letter we have from the Internal Revenue Agent in Charge for January, dated January 23, 1947, concerning the audit of Petitioner's fiscal year ending 1940.

Now, that removes one of our biggest difficulties. We are satisfied to be on a cash basis. In this letter, in connection with the audit for 1944, figuring on a cash basis, the Internal Revenue Agent in Charge states as follows: "For the history of taxpayer see prior agent's reports and U. S. Tax Court's findings of fact in opinion re Birch Ranch & Oil Company v. Commissioner, Docket No. 109993." [13]

That is the one I have been referring to. In the report for the year 1944 Petitioner deducted, showed a loss of \$84,179.37, and here is what the letter states:

"The additional net loss, as shown in this report, is brought about by the allowance in full of amounts paid by the taxpayer in this fiscal year for assessment taxes on Reclamation District 2035." That is \$120,000.00 to enable the district to meet the interest on these bonds.

"A part of the amount paid in this year covers amounts accrued on the corporation's books in prior years, and disallowed in the prior agent's reports as deductions, since the corporation was on a cash basis. For a breakdown of these amounts see Schedule 1-A of this report.

"The findings as shown in this report are discussed with Mr. Robert K. Landrum, Secretary of

the taxpayer corporation, who agreed to all the proposed adjustments shown in this report.”

Now, we have Schedule 1-A, “Adjustments to Net Income, Net Income as disposed by return \$84,-179.37,” which means a loss of that amount. And then it says, “as corrected \$186,899.37.”

The Court: May I interrupt, Mr. Acret? Do I understand you therefore are abandoning the issues as set out as IV (c) in your amended petition on page 3, in which you allege the Commissioner erred in holding that the income—[14] no, excuse me. It is (b) on page 3; IV (b) on page 3.

Mr. Acret: Yes.

The Court: “In disregarding the inventories covering Petitioner’s Conaway Ranch for each of said fiscal years upon the theory that the net income of said ranch is determined upon the cash receipts and disbursements basis, when, in fact, the net income of said ranch, and Petitioner’s entire system of accounting at all times has been and is determined upon its accrual basis.”

I understand now that you abandon that.

Mr. Acret: Yes, I am doing that because I believe we are forced to, and besides that I believe that on the basis of the Commissioner’s findings in that letter, and so forth, if they are satisfied with us being on a cash basis we are, too.

Your Honor, on page 21 of the petition, if you will notice, we ask that in the event any of these errors assessed be disallowed, that we be allowed to carry back the losses from 1944. I will state to your Honor, and I don’t wish to waste the Court’s time

with things we can't do, we can't do anything with reference to the assessment relating to 1941. We only have a right to relief as to 1942, which is the Paragraph (i). The assessment for 1942 is some twelve or thirteen thousand dollars, and we have enough loss in 1944, as approved by the Commissioner [15] in this letter, with all possible deductions under the rules applicable under Section 122 to allow us four or five times the amount of loss necessary to offset this assessment, deficiency assessment for the year ending 1942.

Now, our return for 1944 has never been held in question. There is no deficiency assessment concerning it. All there is, rather than it being held in question, is an approval and increase of that loss we deducted of eighty-four thousand to a net adjustment of the loss to \$102,720.00.

Now, here is what I propose: That the Petitioner be allowed to carry back as much of that loss as may be necessary to meet the deficiency assessment for the year 1942. We abandon any claim on the 1941 because we figure that under our position we can't get anywhere; can't carry back more than two years. That is all that we can carry back to.

Now, I appreciate that the Commissioner might subsequently make a deficiency assessment for 1944, but there is no issue on that yet and this Court could make an order of our right to carry that back, subject to any subsequent deficiency assessments for 1944, that might be assessed. There would be no injustice that way.



The Court: Is there any question at the present time concerning the allowable loss in 1944?

Mr. Acret: I think counsel questions it, and [16] I am submitting the suggestion to counsel that if it develops that the agent in charge's report here, they wish to amend it, and I presume they would have a right to at any time, then this carry-back would be subject to the same adjustment if there was any deficiency. There is no issue before the Court as to the propriety of that loss we have on our 1944 return. If an issue should subsequently arise we would be willing to stipulate this carry-back could—

The Court: Now, do I understand, Mr. Acret, your position is—I state this with a question mark at the end of it—that there is a deficiency in tax of the Petitioner for the year 1941, as determined by the Respondent, in the sum of \$7,833.44, and that there is a deficiency in tax of the Petitioner for the year 1942, ending September 30, 1942, as determined by the Respondent in the sum of \$11,915.67, but as to the tax liability of the Petitioner for the year ending September 30, 1942, the Petitioner is entitled to carry back a loss for 1944; and that therefore the deficiency in the amount of \$11,915.67 does not exist or would not exist or will not exist if the Petitioner is entitled, or is permitted to carry back its loss for 1944?

Mr. Acret: That is an accurate and correct statement of our position, your Honor. Except your Honor did not include the deficiency assessment for the excess profits tax for 1942. [17]

The Court: Yes.



Mr. Acret: That is \$1687.10.

The Court: There is no question now raised as to the deficiencies determined by the Respondent in income tax and declared value excess profits tax for the year ending September 30, 1941, in the respective amounts of \$7,833.44 and \$4,565.41.

Mr. Acret: That is correct, your Honor.

The Court: There is no question as to the amounts of the deficiencies determined for the year ending September 30, 1942, and income tax and declared value excess profits tax, but the Petitioner is now claiming in this proceeding the right to carry back to that year the losses shown in its 1944 return.

Mr. Acret: That is correct, your Honor. And your Honor, I see that the reason we can't do that, if we were on a cash basis, is that the Petitioner did not pay that tax and was unable to pay any taxes until later; and as found and determined by the Internal Revenue Agent in Charge it did pay the amounts as shown here during the year 1944 and paid those in cash. That is the reason the Petitioner's deduction is proper for 1944, if it is on a cash basis.

The Court: Mr. Crouter. [18]

## OPENING STATEMENT ON BEHALF OF THE RESPONDENT

By Mr. Crouter:

If your Honor please, I do wish to make an opening statement on behalf of the Respondent and at the risk of it being a little bit lengthy I would

like to go back into the prior case and try to explain the situation in which we find ourselves in this proceeding.

I gather that your Honor appreciates the situation regarding 1941, and I will come to that. I think that will expedite matters here. Now, on the pleadings as this case stands, if the Court please, you have observed that the proceedings here relates to fiscal years 1941 and 1942. We have deficiency income taxes aggregating \$19,749.11 for both years, and in deficiency and declared value excess profits taxes aggregating \$6,252.51. That is the total for both years.

Now, it might be helpful to the Court for me to make this statement, that I believe you would appreciate, and you might even have the question in your own mind, "Why are we here if we had this prior case before Judge Turner?" It is true there was this prior proceeding of Birch Ranch & Oil Company, this same Petitioner. That case was submitted to the Court out here at Los Angeles on April 5 and 6, 1943.

The findings of facts and opinion came down on the date counsel stated, which was April 20, 1944; approximately a year later.

The case was affirmed on appeal before the Ninth Circuit, the citation being 152 Fed. (2d), 874, and as counsel has stated certiorari was denied by the Supreme Court.

Now in the subject proceeding relative to the years 1941 and 1942, we have similar assignments of error with respect to the accounting basis of

the Petitioner. As counsel has stated, if they were properly on the accruable basis and they were entitled to accrued liability, even though not paid, there might be basis for contending for deductions on that basis. But as I see this situation the prior decision holding that Petitioner was on the cash basis for the prior fiscal years, 1937 and 1939, really in effect controls the accounting question in the subject years, because, as I understand it, about the same system of accounting came through.

So while there is no issue here of *res judicata* raised by either side and strictly that doctrine might not apply, because we have different years, and the facts conceivably could be different. I believe it is the prior decision that compels the results that the Petitioner here for the taxable years, 1941 and 1942, is still on the cash basis.

Now, I believe there will be no question here but Petitioner did not pay any amount whatever as tax or as interest for a period of about 10 years, between 1933 and 1943. That, of course, includes these taxable years.

Now, as I read the Petitioner's pleadings in this case, all assignment of error relating to both years relate to the accounting basis, and this question of taking deductions for taxes or interest accrued on their records.

The right is claimed because of the accruable, and the petition there, I believe, was filed before the decision in the prior case. Now, there was an amended petition here, July 25, 1945. However, that case was still in the courts.

Mr. Acret: I think that was filed within 30 days, that amended petition.

Mr. Crouter: Yes. But the prior case was still on appeal at that time.

Mr. Acret: Yes.

The Court: That is right.

Mr. Crouter: That is the similar position they had in the prior case. I might also state, for the Court's information, and with your permission, I would like to read two sentences from Judge Turner's opinion in the prior case, to show the questions we raise now were not decided there. This is from page 21 of the mimeographed opinion:

"In view of the conclusions reached and the [21] reason therefor, we find it unnecessary to rule on the Petitioner's claim that the bonds of reclamation, District No. 2035, were at all valid and subsisting obligations, consisting of a lien or charge upon the property of the Petitioner so as to entitle it to deduct so much of the amounts paid thereunder as is allocated to interest.

"Neither do we find it necessary to rule on the contention of the Respondent that the owners of the bonds herein question were in reality the owners of the land against which the bonds were issued, and that the bonds do not therefore represent real and actual obligations outstanding."

Now, as your Honor has already perceived, those questions are inherent in the subject case in this respect:—and I believe at this time it would be appropriate, if the Court please, and I now make a motion with respect to the pending proceeding,



Docket No. 8720, and the fiscal year ended September 30, 1941—that the deficiencies in income tax and in declared value excess profits taxes, which are asserted in the deficiency notice, the amounts of which have been previously stated by the Petitioner counsel, be found by the Tax Court and they be sustained on the basis any assignments of error or fact alleged in the petition have now been conceded, abandoned or withdrawn, in effect, by the Petitioner, so that there is no issue or no necessity of going into that matter further. I would like to have that motion of record.

The Court: The Court will take it under advisement.

Mr. Crouter: Now, with respect to the fiscal year, 1942, the situation is very similar with one exception, if the Court please. As I read the petition there is no assignment of error whatever relating to 1942, and to any error of the Commissioner, except this accounting question and the question of accrual or cash basis. I believe that counsel for Petitioner has now conceded that for both years Petitioner is conceding to be on the cash basis, as previously held in the prior case. And since there is no error whatever relating to any action of the Commissioner with respect to 1942, I move that decision be entered in favor of the Respondent for the fiscal year 1942 for both the income tax and declared value excess profits tax deficiencies in the amounts asserted in the deficiency notices, which amounts were previously stated by the Court.

The Court: Motion taken under advisement.

Mr. Crouter: I might say in that connection, if the Court please, there is only one matter in the petition that I can see that conceivably refers to this 1944 carry back question. In the statement of facts, I believe I can [23] cite your Honor the exact place where that occurs.

Mr. Acret: Is it page 18, counsel?

Mr. Crouter: Yes. Thank you.

On pages 18 and 19 of the printed amended petition, subparagraph (i),—now, mind you, if the Court please, this is all a part of a statement of facts which is really repeated by reference starting at page 16, but it all refers back to the commencement of Petitioner's allegations of fact; that is V, page 4.

“The facts upon which the Petitioner relies as a basis of this proceeding are as follows:—”

Then we go down through considerable setup of facts for the first year and a repetition starting at page 16 for reference, then with new paragraphs, and the last one is subparagraph (i) of pages 18 and 19. That relates to an alleged net loss for 1944.

The same fiscal year ended September 30, 1944, which, under the two-year provision of Section 122, relating to carry-back, I assume Petitioner now desires to have carried back, and asserted for 1942.

Respondent on time and as soon as this petition was filed denied the allegations of fact, including subparagraph (i). I don't believe there is any question about that. That has been denied, since the Respondent's answer was filed on August 29,

1945. That remains denied, and that is still [24] Respondent's position.

Now, with respect to these other losses referred to in that subparagraph (i) at the top of page 19, Respondent does not contest other losses or deductions, except on account of this bond situation.

As I see this case, we still have undecided and pending for the Court's decision, if we have to go into that here, the question of whether Petitioner is entitled to deductions for this tax or interest. I think there is a very serious question whether that matter is properly before the Court. I believe that counsel has referred to that previously, in saying he appreciates there is no issue here regarding 1944.

Now, it is contended for administratively, and has been under consideration administratively, that is not final. It is not conceded that the Petitioner is entitled to those deductions, as counsel said, the statutes are still open. That is still a matter for the Bureau of Internal Revenue for the prior years, 1941 and 1942.

If the Court rules that is a pending issue in this case and is properly before this Court and this is the appropriate time and place to go into it, the Respondent is prepared to go through and litigate that question.

The Court: What question, Mr. Crouter?

Mr. Crouter: The question of the right to carry back an operating loss from 1944 to offset the deficiency for 1942. As I understand, that is counsel present position.

The Court: Turning to pages 18 and 19, does

Respondent deny—I know that Respondent has denied in the pleading—does Respondent now at this hearing contest and deny the fact that losses in the amounts stated were sustained by the Petitioner in its fiscal year ended 1944?

Mr. Crouter: Yes, we do, if the Court please.

The Court: Only \$121,084.38?

Mr. Crouter: There are different amounts, because of the accounting basis. The return for that year, as I understand, claimed a deduction for tax of \$123,666.17. On account of the reclamation bonds.

The Court: The losses itemized on pages 18 and 19, as I understand it, were not on account of taxes but were by reason of drilling and abandonment of an oil well as were other itemized losses appearing on 19.

Mr. Crouter: Yes.

The Court: Those are alleged in the amended petition, a total of \$121,084.38.

Mr. Crouter: I believe Petitioner's position is he still claims losses based on these taxes in addition to those items which are specifically enumerated. You see, he does have the total figure right at the last line on page 18, contending for a net loss of seventy-three thousand [26] plus. And that is arrived at through various other adjustments, but they include, it is my understanding they include an item based upon these alleged taxes.

The Court: Is that correct, Mr. Acret?

Mr. Acret: Yes, your Honor. Then when we were put on the cash basis the Internal Revenue



Agent in Charge—because we paid some two hundred twenty-one thousand in taxes that year in cash—he changed our net loss to \$120,000.00, I think it is, by that statement.

It is true this petition was made before we had to concede we were on a cash basis, and it changes the amount of our net loss to the basis stated in this letter. This letter concedes the payment of \$221,610.00 paid by certified check as taxes to the County Treasurer during the year 1944. That in itself is part of our return. We paid that amount or would be on a cash basis, on an accruable basis; we just deducted \$123,666.17. Now, that alone is sufficient to give us a carry-back.

The Court: Then the existence of a loss subject to carry-back depends upon this tax deduction allowed in this tax payment allowed in 1944, is that correct?

Mr. Acret: Yes, your Honor. We contend that in 1944, due to change in circumstances, there is no issue as to that, and if any issue subsequently arises we are willing to have this carry right to the carry-back [27] determined by the final determination of that question, when the issue of 1944 does arise.

Now, all we have is a statement of the Agent in Charge approving our payment of taxes in two hundred twenty-one thousand and our deduction of that. They themselves on their accounting rendered to us include that in the net loss they credit us with.

The Court: As I understand, now, Mr. Acret, all you want is an order now in this proceeding that you are entitled to a carry-back if, as and

when it is determined that there is a net loss, subject to a carry-back in 1944, is that right?

Mr. Acret: That would be the effect of it. That is on the theory your Honor has jurisdiction now to grant this right to carry back. If it weren't granted now we would lose all our right to relief.

The Court: And if it should develop there is no loss subject to carry-back, you would get no relief.

Mr. Acret: That is right. That would only be common justice, to have that provision.

The Court: How do you anticipate that question will be decided?

Mr. Acret: It will be decided if and when the Commissioner changes his mind as to this statement rendered and instead of rendering this statement approving the return [28] assesses a deficiency for 1944. That is all. Then there will be precise issues which we can then meet on the cash basis. As it is, when we started this we were all at sea. As Judge Turner said, he didn't decide whether they were on accrual basis or cash basis. He decided we were on a cash basis with reference to the Conaway Ranch.

The Court: I think we interrupted Mr. Crouter.

Mr. Crouter: I would like to say, about the question discussed with counsel, I don't think there is any misapprehension or misunderstanding regarding the position of the Respondent, as exercised by the Technical Staff here at Los Angeles as far as the Court observes, from the calendar, this case was on the prior calendar we had this spring. It was continued over from that calendar, particularly be-

cause of this net loss question, so both sides would have an opportunity to go over and consider it. I don't want the Petitioner to have any misunderstanding about the position of the Respondent on this question. It is my understanding the Bureau of Internal Revenue and the Commissioner do seriously question and are inclined to, and disallow this carry-back based on the bond question; and at the years 1941 and 1942, which are before the Court now. I know that some things are subject to administrative adjustment. After the decision, whether a net loss carry-back properly could be, even after the Court decided this [29] question on the issues presented, it might be subject to adjustment. I am not intimating and my own guess is the Commissioner would not allow any adjustment administratively, such as the Petitioner now claims, based on a net loss carry-back for 1944. This question has been up and discussed by the staff. Counsel has been informed long prior to today we do not concede that point and we do not concur in his position.

In other words, I think I should go further with my opening statement, as I previously planned to and tell the Court the basis and reason for that. Fundamentally it breaks down to two questions. I might, in the first place, say there is very serious question in Respondent's mind as to whether there was any real tax or any real interest paid here, for which a deduction should be allowed or recognized under the Internal Revenue Code. We have a very

unusual situation, in that it is a closely held corporation.

It is my understanding, although there might be some slight discrepancy, Mr. Birch and his wife owned entirely and they have for years owned entirely the Petitioner corporation. We have these bonds held by Mr. Birch. We have the land owned by the corporation. We have a situation here, if the Court please, where the Respondent contends there is no real liability for paying any amounts of interest or taxes, so that there is no real foundation for the [30] claiming of deductions.

Now, that breaks down into several points or facets, I might say. If we go into this question here I think it will be clear and no doubt whatever for this period of 10 years, from 1933 to 1943, no payments whatever were made, no demands made. That indicates somewhat the question whether there was any real legal liability. The story there is a rather long one and I will not try to cover all the facts in the opening statement.

On the question of liability there are a number of things I would like to mention, if the Court please. And I am referring now to the question of these deductions claimed for 1944; bring it right down to date. Respondent's position is there were no valid bonds outstanding in 1944 which required any payments of interest or taxes. And that there were no real lien on property which required the making of such payments. I might also state it is my view and I will attempt to show these payments were made——



The Court: May I interrupt again, Mr. Crouter? I am sorry to interrupt. I want to get these things straightened out. When you are speaking about the Respondent's position, you are speaking about the Respondent's position as you know it at this time, and not with reference to the Revenue Agent's report which is referred to by Mr. Acret?

Mr. Crouter: That is correct. [31]

The Court: And you are not referring to any formal determination of the tax liability of the Petitioner for the year 1944, as I understand, as there has been no determination of deficiency or final action taken by the Respondent with regard to that.

Mr. Crouter: That is correct, if the Court please.

The Court: You are speaking now of the Respondent's position as to this case.

Mr. Crouter: That is correct, and particularly in support of our denial of the allegations under the fact they are including in the allegations there was a net loss for 1944. That is, it is very meager and it is very thin. There is that allegation in the petition and that has been denied. I am arguing in support of all our grounds to support that denial.

As the second point on the question of liability, Respondent contends where we have a complete ownership of the individual and the corporation, the individual owning the bonds and the corporation owning the land, and that there is no real issuance of bond, that bonds are not held by a third party, an arm's length transaction, there again we have a sort of merger of the individual and his

corporation, so even if there were any liability at any time it would be merged. When that situation arose, as we may show in this case, there was an acquisition by Mr. Birch of all of the [32] bonds which were outstanding, even in addition to those which he did not acquire at their inception. I believe he and his wife held most of the bonds right from the beginning. They had contracts and arrangements and agreements whereby they would own and control this entire situation. I might clarify one part, if the Court please.

Mr. Acret: I was going to say, you won't have to show—I will concede all these facts. They are not in question.

Mr. Crouter: I would like to clarify one thing, if the Court please, and that is, this was not an active reclamation project instituted and carried out at the time the Petitioner was formed or at the time these bonds were issued. As I understand, the actual reclamation work forming the basis of all this was long before this reclamation district was organized and bonds issued to the tune of about \$2,000,000.00, and then on certain dates in 1944, four different dates on some subsequent dates, amounts were routed through the County Treasurer's office. He was an officer of some kind of the reclamation district, also.

I wish to get this picture across to the Court. On a certain date an amount usually close to \$60,000.00, sometimes a little less, sometimes a little more, would be paid into the County Treasurer's office. He would immediately draw a check payable to the

holder of the bond. So that we [33] do not have payments of taxes or payments for work undertaken in a real sense. We have an exchange of moneys through the County Treasurer's office, and that is the best that the Petitioner could show here with respect to payments of the so-called obligations. That runs right to the question, as the Court will perceive, of the relationship of Mr. Birch and his corporation. There is a question here, and I will confess it isn't clear in my mind, if the Court please, and I have not been able to see or examine the original evidence, as to what bonds, if any, were really outstanding during the 1944 period. The original issue was 1925, and it has been contended that there was a re-issue or a refunding operation, and then a second re-funding operation. I am not certain whether counsel contends they were bonds of the second re-funding operation or the third re-funding operation, which were outstanding, on which they claim they made payments in 1944. But even if bonds were drawn up and names put on them, and they were on the face of it issued, I don't believe they have any higher standing than the original.

I might say it really stems, as I see it, from the organization of the reclamation district and Mr. Birch was given a county warrant for \$2,000,000.00. He received this—Mr. Birch and others, I should say, Mr. Conaway, in particular—I believe it is his father-in-law—they [34] received this warrant that was not for cash put in. That was on account of reclamation done years before. That was the con-

sideration for it. That warrant was not left outstanding. The warrant was almost immediately cancelled of record and the warrant was exchanged, given back to the officials of the accounting and reclamation district, and the bonds were received in lieu of the warrant.

Now, as Respondent sees this, if the Court please, it is difficult and almost impossible for us to see that these bonds had any purpose whatever, affected anything at all except taxes. They did not affect actual operations. They did not affect any real excavation work or reclamation work. They did not create this system and situation whereby at first merely accruals were put on the record, deductions claimed for accruals. There was no money moving whatever at first. The returns were questioned and it was litigated and, as counsel stated, the decision of the Tax Court required actual payment. After that date we have the form of payment going through. Respondent contends the result is no different, in effect, as Mr. Birch is taking out of one pocket and putting in another, and is not the proper basis for a tax deduction.

To go on with some other point here, I will be as brief as I can. I think the facts will show, if we get into the question, oftentimes the parties would go to a [35] bank and borrow enough money so that they could make out a cashier's check, which would go to the Treasurer, and then he would hold that check and in exchange for it he would issue one purporting to pay bonds, coupons. All of this, I might say, is not principal. The principal amount



has never been changed, as I understand it. This all relates to interest, which is supposed to have been paid on the original assessment or situation arising out of the creation of the district and issuance of the bonds. I believe the record will be clear, in spite of what my good friend Mr. Acret says, there is no real tax angle. It was interest on that original obligation, if there was any. By the same token, it is interest on the coupons. About the same rate applies, 6 per cent, through here. We will have \$60,000.00 payment going through the Treasurer's office, ostensibly as an assessment or claim made by the county, and then the Treasurer pays out 6 per cent interest, which would be \$60,000.00. And that would be received by Mr. Birch as tax exempt interest. It involves the question of the law and regulations of tax exempt interest, with respect to moneys from a municipality. That is the way this thing has operated for years, if the Court please.

The Respondent's position is that the whole corporate entity of the Petitioner, particularly, should be entirely disregarded. That for all tax purposes the [36] corporation and Mr. Birch and his wife are one and the same thing. There is no real substance to the transactions giving rise to the deductions. Therefore, the Respondent contends that particularly in this proceeding relating to the years 1941 and 1942, first, there is no real issue or question before the Court showing error in the Commissioner's determination. And even if this 1940 allegation is relied upon there is no merit, no basis

in that and certainly it has not been shown, up to this point, that there is any basis for, that any legal liability or obligation calling for such payments, there is a serious question as to whether Petitioner actually made those payments. I do not even concede that.

The Court: Well, Mr. Crouter, as I understand the petitioner's position, it is that in 1942, Petitioner concedes that there are the deficiencies in income tax and excess profits tax, as determined by the Respondent, but prays an order of this Court in this proceeding, and which would be a part of the order fixing the amount definitely of the deficiencies to the effect that the Petitioner shall be entitled in a computation of its tax liabilities for the fiscal year ended September 30, 1942, to the carry back of a loss sustained in 1944, if it shall be finally determined in the proper proceeding that there is a loss in 1944.

Now, I take it, that such an order in this [37] proceeding would not be binding as to any question later arising with regard to the 1944 tax, but would merely safeguard the Petitioner as to 1942, in the event that there should be found a loss subject to carry-back in 1944. It would certainly seem to me premature in this proceeding to litigate a matter which has never passed through the final determinative processes of the Respondent, as to 1944. And it is hard for me to find how there is really much difference between the parties in this proceeding, which is the subject of litigation here.

Mr. Crouter: If the Court please, I don't mean to gloss over that. I appreciate the Court's position there. It seems to me, under my understanding of Section 122, it is quite possible or even probable that the 1944 question could be handled in that manner. As I recall, though, and I am just going by memory, I should have brought the code number, Section 122 (g) has a provision that decisions are subject to later renew or adjustment because of a net loss carry-back.

The Court: I admire counsel's temerity in even attempting to quote from 122 or 121, or any of those allied sections. That is 122 (g), you say?

Mr. Crouter: I appreciate I am hazarding a great deal.

Mr. Acet: I think your hazard is correct. I think that is correct, 122.

The Court: I think counsel had better look it up. I can't find it.

Mr. Crouter: We will be glad to go into that. I can appreciate this question quite possibly could be settled administratively between the Commissioner and the Petitioner here for the year 1944 or we might find ourselves back before your Honor or some other Judge litigating the 1944 case.

I can appreciate that properly belongs to a 1944 adjustment.

The Court: It would seem to me, while I appreciate from the statement of counsel that the question is a very interesting question, and I had a little bit of that problem in the Adler Realty Company case in which I finally ended up writing the dissent, but

it is a rather interesting problem. But I don't see how it can very well be presented in this proceeding.

Mr. Crouter: I had serious doubt about the jurisdiction. That is the reason I wanted particularly to point out the exact status of the pleadings here.

The Court: I do think that perhaps the pleadings are sufficient to justify the entering of an order of the kind outlined, that is, saying there is a deficiency subject to adjustments on account of a necessary loss [39] carry-back, if any.

Mr. Crouter: Yes.

Mr. Acret: Yes.

The Court: I would certainly not want to determine that in this proceeding. Now, I don't want to urge counsel to act unduly hastily in this case, because in matters of procedure one error can lead to an awful lot of resulting errors.

Do counsel feel there should be any evidence submitted in this proceeding?

Mr. Acret: I do, your Honor.

The Court: Such as the introduction in evidence of the findings of fact and opinion in the Turner case?

Mr. Acret: Here is what I propose to do, and I think possibly it would be agreeable to counsel, is to put in this letter, which establishes our information to date, and the findings of fact referred to in the letter, and a photostatic copy of our tax return showing the loss of \$84,000.00, and the virtual approval of that loss and increase of the loss by the position taken at this time by the Internal Re-



venue Agent in Charge. I think that is sufficient to give the Court jurisdiction to keep us open, the right to the carry-back. That is all. Automatically, if they don't go further with it, why, that will be sufficient. If they do go further with it, in common justice they are [40] protected; nobody is hurt. There is no issue as to 1944 that is before the Court or that we would be obliged to meet at this time.

Mr. Crouter: I might say, if the Court please, it isn't clear to me that would be a good method of procedure here. Certainly, on behalf of the Respondent, if the Petitioner admits, to go into the merits of the question of 1944 I must certainly protect myself and put in a good deal of evidence. We will find ourselves litigating the 1944 question.

The Court: I understand the Revenue Agent's letter, to which counsel refers, will not be submitted as proof to any of the facts set out therein or the existence of the losses referred to, but merely to prove that at the present time there has been an official recognition on the part of the Respondent there may be a net loss allowed in 1944.

Mr. Acret: That is it exactly. Further than that counsel doesn't need to worry, we are conceding the matter may be left open. We are conceding it isn't any decision on the merits.

The Court: It is obviously a matter of law. The Revenue Agent's report is the tentative proposition——

Mr. Acret: Yes.

The Court: ——and it must be construed in the

light [41] of the statements made by counsel for the Respondent that at the present time, so far as the Respondent counsel knows, the re-disposition with regard to 1944 is contrary to that taken by the Revenue Agent in the report referred to.

Mr. Crouter: That is correct. I wanted to clear it up. That is not agreed to by Respondent, as having any evidentiary value.

The Court: The Respondent does not agree that that now represents the Respondent's position on it, and the Respondent counsel does not agree any of the facts therein contained are true, but the Respondent does not deny, however, that that letter was written.

Mr. Crouter: That is correct.

The Court: Yes.

Mr. Acret: That being the case, we offer in evidence at this time the letter from the Internal Revenue Agent in Charge dated January 22, 1947, with three pages attached thereto.

The Court: I take it that that is offered in evidence for the purpose of showing that as of the date of that letter the Commissioner of Internal Revenue recognized there was an allowable net loss for the year 1944, is that correct?

Mr. Acret: That is right.

Mr. Crouter: And if the Court please, I will [42] object to that on the ground it is irrelevant and immaterial under the issues in this case. It is not final and there is no basis of estoppel or final action shown by the letter.

The Court: Objection overruled. Admitted for the purpose stated.

Mr. Acret: May we substitute a photostatic copy?

The Court: Leave granted.

The Clerk: Exhibit 1.

(The document above-referred to was received in evidence and marked Petitioner's Exhibit No. 1.)

The Court: It may be withdrawn and a photostatic copy substituted.

Mr. Acret: At this time we offer the findings of fact of the Tax Court in Docket 109993, excluding therefrom my pencil marks which are not a part of the exhibit.

The Court: Is there any objection?

Mr. Crouter: If your Honor please, yes. This involves a question which I don't want to prolong the proceedings with, but there are one or two things in there, if the Court please, I believe are inadvertent and they are not real facts. They are references to payments which were during that period when no payments were made. It may be based upon the testimony in the prior hearing. I know that the findings in the main are accurate and covers the picture. There are certain things in that that may prejudice [43] the Respondent's position. I cannot concede all those facts stated there are true and correct. I am prepared in this proceeding to prove the contrary to some of them.

I object on the ground they are references to

state court proceedings, which, as a matter of fact, were not real adversary proceedings. Respondent excepts and objects on that ground. I have prepared a summary of all the findings with the exception of the two matters I mentioned and agreed to stipulate with counsel to, in the event we proceeded. Those are the facts we would agree to. I have no objection to the findings and opinion going in for the information of the Court. I can't agree to the facts.

The Court: I question how important any of those facts contained in the memorandum and opinion and findings are in this case. Ultimately the question I have is a procedural question.

Mr. Crouter: I appreciate that, if your Honor please. We go from case to case. I don't want to be confronted with a 1944 case, particularly if I should be handling this, that back in 1947 I agreed those were facts.

The Court: Has counsel for Petitioner examined the summary of the facts mentioned by counsel for the Respondent?

Mr. Acret: I discussed them over the telephone with [44] counsel, and I understand he wanted to stipulate as to facts with certain conditions added to it, at least. Over the telephone I couldn't agree to that. But I would like to call your Honor's attention to the fact these findings of facts are the findings of fact referred to in Exhibit 1. Properly they should be supplemental to Exhibit 1.

Mr. Crouter: I have no objection to that going in merely for the Court's information and for consideration in making its ruling and order with



respect to the net loss carry-back question. I do not concede all the matters stated there are facts, and I do not wish to have the Commissioner prejudiced in any future proceeding of any kind in court or out with respect to anything I do now regarding this statement.

The Court: Well, I think that will have to go in in one way or another, for one purpose or another, that findings of Judge Turner.

Mr. Crouter: Yes.

Mr. Acret: Whatever the legal effect of that is is another matter that results just as a matter of law.

The Court: I will overrule the objection and it will be admitted in evidence.

The Clerk: Exhibit 2.

(The document above-referred to was received in evidence and marked Petitioner's Exhibit No. 2.) [45]

Mr. Acret: We offer in evidence at this time photostatic copies of Petitioner's income tax return for the fiscal year ending September 30, 1944.

The Court: Is there any objection?

Mr. Crouter: No objection to that.

The Court: It will be accepted in evidence.

The Clerk: Exhibit 3.

(The document above-referred to was received in evidence and marked Petitioner's Exhibit No. 3.)

Mr. Acret: With that Petitioner rests, upon the

request heretofore made in the opening statement that the Court allow the matter to be kept open upon the conditions heretofore stated by the Court.

The Court: I have as part of the record two motions made by the attorney for the Respondent squarely asking for the determinations of deficiency by this Court, as determined, which I took under advisement.

I think it might be well, in view of the rather unusual character of the motion made by you, Mr. Acet, that it should be reduced to writing and filed.

Mr. Acet: Yes. I am sure counsel and I can agree on it.

The Court: So I will have before me exactly what Petitioner suggests in this matter.

Mr. Acet: Counsel is easy to work with. [46] Nevertheless, we can get something out that will be agreeable.

The Court: Mr. Crouter, do you have any matters?

Mr. Crouter: No. If the Court please, in view of my understanding—and I want to briefly refer to that—this is not in any way, or any sense to be taken as an adjusting of 1944 fiscal year on the merits, but merely to hold open this question of carrying forward. Respondent does not offer evidence at this time.

The Court: I think it would be very difficult for me, on the facts I have before me, to make any determination. I don't see how I would really. I don't see at the present time the jurisdiction that I would have.

Mr. Crouter: Yes. I don't want anything to be construed against me by my silence.

The Court: It seems to me the only question I have to determine is do I, under the pleadings and the facts that are before me, have the right to make, in effect, a determination of deficiency, to enter an order re-determining the deficiency in the amount as determined, with a conditional qualification, so to speak, that in the ultimate amount to be paid by the Petitioner credit shall be given on account of a possible loss carry-back for 1944, in an amount which has not yet been determined and which I do not attempt or in any way purport to determine. [47]

Mr. Acret: That is it exactly.

The Court: In my experience there has never been such an order issued. It may well be under the statute such an order can be issued. So far as I know it has never been determined. Are counsel familiar with that?

Mr. Acret: I feel satisfied, your Honor, I have made some search. There is no precedence for it. There is no precedent for the particular situation we find ourselves in. Section 122 is, I am sure, one that leaves us the right to relief and if your Honor makes that open, why, it will keep the right to relief open.

The Court: But then the question comes up, assuming that you have the right to relief, what kind of relief is it, administrative relief which has to go through the Bureau of Internal Revenue, or is it a relief which can be prescribed in an order by

this Court, and that is something I don't know about.

Mr. Acret: Your Honor, it clearly is relief that may be prescribed by this Court. We made the necessary allegations and we asked in our petition for relief by the Court. If it weren't done in that way I don't think that we would be protected. It would be a jurisdictional question. The only reason we can be granted relief is we are before the Court with that question. We are before it with the facts alleged, for a relief prayed for. The alternative, [48] if we don't get the relief made under the errors assigned—there was no error made by the Commission—the fact we have a right to carry-back because of errors by the Commissioner, therefore, we couldn't assign an error.

We had a right when we brought this petition, and I take credit to myself for foreseeing this possibility, that we might not get anywhere with the Supreme Court, but, in any event, if we got the matter before the Court, this Court would then have jurisdiction to do justice and grant us a relief to any carry-back that it would appear we are entitled to.

So it is a question of relief by an order of the Court. That is what we are here for. We ask for that. The Court has jurisdiction to do that very thing.

The Court: As I understand it, the Petitioner rests?

Mr. Acret: Yes, your Honor, we rest.

The Court: And Respondent rests?



Mr. Crouter: That is correct. In response to your Honor's inquiry, I might say this: I don't know as it will have a great deal of effect on this. This question came up in connection with stipulated questions of corporate excess profits, particularly, and pursuant to instructions of our office in some of the stipulations we have included a provision that the deficiency so agreed upon is subject to [49] adjustment for any net loss carry-back, if any. That is being worked out, but I have never had a case exactly like that. I am content to submit this case under the circumstances your Honor has stated.

Mr. Acret: The Commissioner himself could grant administrative relief in addition, but the relief from your Honor is an order by the Court. It is our contention, I respectfully submit, your Honor.

The Court: The briefs will really not be elaborate briefs, in that there will not be much discussion of the facts. It will really be in the nature of memorandum more than briefs. I do think probably briefs should be filed, unless counsel can get together and agree.

Mr. Crouter referred to the evolution to administrative procedure in this matter. It might be that the evolution will disclose, say, a policy which will permit counsel to agree upon an order to be entered in this case.

Mr. Acret: What I was trying to do, your Honor, and I appreciate the situation that you are in, and the hundreds of these matters, was to get one of these that could be disposed of right now in a

clear cut manner so you won't have this one on your neck, at least, from now on. That is all. It could be disposed of without briefs or anything else, and it is one you wouldn't have to take home with you. [50]

The Court: Well, I, of course, would like it at the present time, and I think counsel are entitled to indicate their positions in briefs, so I will just make an order that briefs may be filed pursuant to the rules.

Mr. Acret: Very well, your Honor.

The Court: I again suggest to counsel for Petitioner that a written motion be filed embodying the matters outlined in your opening statement.

Mr. Acret: Yes, your Honor.

Mr. Crouter: Thank you.

The Court: Thank you.

(Whereupon, at 11:25 o'clock a.m., Monday, June 30, 1947, the hearing in the above-entitled matter was closed.)

Filed T.C.U.S. July 22, 1947. [51]

[Title of Tax Court and Cause.]

## MEMORANDUM FINDINGS OF FACT AND OPINION

Kern, Judge:

Respondent determined deficiencies in petitioner's income taxes and declared value excess-profits taxes for the taxable years ended September 30, 1941 and 1942, as follows:

Year	Income Tax	Declared Value Excess-Profits Tax
1941.....	\$ 7,833.44	\$4,565.41
1942.....	11,915.67	1,687.10

In its amended petition filed herein on July 25, 1945, petitioner alleged that the respondent erred in determining these deficiencies; and among the errors set out in the petition alleged that respondent erred in determining that petitioner was on the cash receipts and disbursements basis, and in disallowing "the deduction (claimed as taxes) of \$120,000 interest on \$2,000,000 of bonds issued by Reclamation District No. 2035 \* \* \* ."<sup>1</sup> In paragraph V (i) of the amended petition the following allegation of fact was made:

That during petitioner's fiscal year ending September 30, 1944, petitioner suffered a loss in the sum of \$73,556.88 by reason of the drilling and abandonment of an oil well known as the Stovall-Wilcoxson well, and the leasehold interest in connection therewith; that in the same year this petitioner suffered

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<sup>1</sup>The quoted language is taken from the notice of deficiency.

losses from sales of property other than capital assets as follows:

A 338-acre farm situated in Stanislaus

County, California.....	\$36,417.50
Lots 61, 112, 141, Tract 993 .....	1,160.00
Lots 32, 36, 60, 91, Tract 993 .....	1,520.00
Lots 87, 62, 189, 90, 108, Tract 993.....	1,730.00
Lot 201, Tract 993 .....	1,200.00
Store Building, 320 Venice Blvd., Los Angeles .....	5,500.00

that in its income tax return for said year petitioner listed and deducted all of the aforesaid items of loss in the total sum of \$121,084.38; that should this court deny any part of this petitioner's petition herein this petitioner desires to carry back to its fiscal year ending September 30, 1942, as much of said losses in the said sum of \$121,084.38, up to \$25,000.00 thereof, as may be necessary to offset any part of the said tax deficiencies involved herein.

In paragraph (i) of the prayer of the amended petition, petitioner asks as follows:

That should this court deny any part of this petitioner's petition herein that petitioner be adjudged entitled to carry back to its fiscal year ending September 30, 1942, as much of said losses in the said sum of \$121,084.38, up to \$25,000.00 thereof, as may be necessary to offset any part of the said deficiencies involved herein.

Respondent denied the material allegations of petitioner's amended petition by answer filed on August 29, 1945.



At the hearing held herein on June 30, 1947, counsel for petitioner conceded that there were deficiencies in tax as determined by respondent, but asked that the Court, in its decision to be entered in this proceeding, provide by order that the petitioner should be entitled, in computing its tax liability for the fiscal year 1942, to the carry-back of losses sustained in 1944, if it should be determined in the proper proceeding that there were losses in 1944 subject to carry-back. Respondent moved orally that a decision be entered in favor of respondent in the amounts of the deficiencies determined by him as to each of taxable years here involved. These motions taken under advisement.

Petitioner concedes that no net operating loss from 1944 may be carried back to 1941. As to petitioner's fiscal year ended September 30, 1941, and the deficiencies determined by respondent in petitioner's taxes for that year, respondent's motion is granted.

Upon brief the petitioner's position is stated as follows:

We respectfully submit that respondent's motion as to the determination of the deficiency for 1942, ought to be denied and that petitioner on the other hand ought to be granted temporary relief herein by this court's determination (in lieu of the granting of a motion) as follows:

1. That petitioner is entitled to carry back to the year 1942, such operating loss as it may have suffered during the year 1944.

2. That the existence of such operating loss for the year 1944 cannot be determined in this proceeding.

3. That the question of petitioner's right to a re-determination of the deficiency assessment for 1942 be held open until the commissioner's determination of the existence or non-existence of such operating loss shall have become final, or shall have become lost by the running of the statute of limitations.

At the hearing herein petitioner introduced in evidence its income and declared value excess-profits tax return for the fiscal year ended September 30, 1944, which showed net income in a minus figure of \$84,179.37 and reflected the loss alleged in the petition, a report of the internal revenue agent in charge, Los Angeles Division, covering the examination of its income tax return for that year, and the Memorandum Findings of Fact and Opinion entered by this Court on April 20, 1944, in the case of Birch Ranch and Oil Co., Docket No. 109993, which involved the tax liability of petitioner for the years 1937 and 1939. The report of the internal revenue agent made no adjustments with regard to petitioner's tax liability for the fiscal year 1944, but in the statement attached thereto adjusted the net income as disclosed by the return by increasing the net loss from \$84,179.37 to \$186,899.37. The report contains the following statement:

The additional Net Loss as shown in this report is brought about by the allowance, in full, of amounts

paid by the taxpayer in this fiscal year for assessment taxes on Reclamation District #2035. A part of the amount paid in this year covers amounts accrued on the corporation's books in prior years, and disallowed in the prior Agent's reports as deductions since the corporation was on a cash basis. For a breakdown of these amounts see Schedule 1-A of this report.

The findings as shown in this report were discussed with Mr. Robert K. Landrum, Secretary of the taxpayer corporation, who agreed to all the proposed adjustments shown in this report.

At the hearing herein counsel for respondent reaffirmed the denial contained in his answer relating to the ultimate fact of petitioner's operating losses for 1944, and stated that the report of the internal revenue agent in charge did not represent the respondent's position with regard thereto.

Respondent, on brief, contends that there is no evidence in the record upon which a finding can be made as to the amount, if any, of net loss carry-back from 1944 to 1942, to which petitioner is entitled; that this is an issue raised in the pleadings upon which petitioner has the burden of proof; that there has been a failure of proof; and that, since petitioner concedes the correct determination of the deficiencies for 1941 and 1942 (aside from the question of the net loss carry-back) unconditional and immediate decisions should be entered for the full amount of the deficiencies as determined by the respondent.

As we have pointed out, petitioner on brief takes the position "that the existence of [the] operating

loss for the year 1944 cannot be determined in this proceeding," while the respondent's position on brief is equally explicit that the operating loss for the year 1944 sought to be carried back to 1942 is an issue in this proceeding and must be decided herein.

The respective positions of counsel were not so definitely stated at the time of the hearing herein. Although the opening statements of counsel for the parties were quite long, it is not clear from a reading of the transcript, and was not clear at the trial, what their several contentions were. A fair statement of petitioner's position at the trial seems to be as follows: While certain allegations were made in the petition as to an operating loss in the taxable year 1944 which should be carried back to 1942, the only issue in this proceeding with regard to such a carry-back was the good faith of the petitioner in claiming it and the probability of its existence. The question of whether there was such an operating net loss in 1944, and its amount, would be decided on its merits in a proceeding involving the taxable year 1944, and only after that year had been considered administratively and with finality by the respondent, as by the issuance of a deficiency notice relating to that year. Pending such administrative action and a hearing on the merits as to the net operating loss for the taxable year 1944 in a proceeding relating to that year, petitioner requested an order in this proceeding safeguarding its right to a carry-back of such a loss, if, when and to the amount it was ultimately established.



Respondent's position at the trial seems to be fairly reflected by the following excerpt from his counsel's statement:

The same fiscal year ended September 30, 1944, which, under the two-year provision of Section 122, relating to carry-back, I assume Petitioner now desires to have carried back, and asserted for 1942.

Respondent on time and as soon as this petition was filed denied the allegation of fact, including subparagraph (i). I don't believe there is any question about that. That has been denied, since the Respondent's answer was filed on August 29, 1945. That remains denied, and that is still Respondent's position.

Now, with respect to these other losses referred to in that paragraph (i) at the top of page 19, Respondent does not contest other losses or deductions, except on account of this bond situation.

As I see this case, we still have undecided and pending for the Court's decision, if we have to go into that here, the question of whether Petitioner is entitled to deductions for this tax or interest. I think there is a very serious question whether that matter is properly before the Court. I believe that counsel has referred to that previously, in saying he appreciates there is no issue here regarding 1944.

Now, it is contended for administratively, and has been under consideration administratively, that is not final. It is not conceded that the Petitioner is entitled to those deductions, as counsel said, the statutes are still open. That is still a matter for the

Bureau of Internal Revenue for the prior years, 1941 and 1942.

If the Court rules that is a pending issue in this case and is properly before this Court and this is the appropriate time and place to go into it, the Respondent is prepared to go through and litigate that question.

The judge presiding at the hearing was not asked by either party during the hearing to rule, and did not then rule that the question of the existence and amount of the net operating loss carry-back from 1944 was an issue pending in the case, and one which should have been litigated in this proceeding. While he made no ruling on the question, he did indicate a reluctance to go into the question on the merits in the instant case, pointing out the difficulties incident to the judicial determination of the taxpayer's tax liability for one year by the determination of its net income or net operating loss for a later year which had not been subject to complete administrative audit and review, when the facts necessary to such determination were disputed by the parties. Cf. *Uni-Term Stevedoring Co.*, 3 T. C. 917; *Pioneer Parachute Co.*, 4 T. C. 27.

This recitation of the proceedings at the hearing herein necessary to present in a fair and complete manner the question which is now before us. That question, stated broadly, is whether the existence and amount of taxpayer's net operating loss for one year may be and, in this case are, issues to be determined by this Court in a proceeding involving its tax liability for a prior year to which the net oper-

ating loss for the later year is sought to be carried back, when the years in questions are not those covered by Section 3780 of the Internal Revenue Code.

It should be noted that sections 3779 and 3780 of the Internal Revenue Code, added by section 4 (a) of the Tax Adjustment Act of 1945, are not available to petitioner since they are applicable only to taxable years ending on or after September 30, 1945, and the net operating loss, sought to be carried back in the instant case is from the taxable year ended on September 30, 1944. If section 3780 had been available to petitioner it might have filed its application for a tentative carry-back adjustment of the taxes for the taxable year 1942 at any time within a year after the end of the year 1944 and might have thereby forced the Commissioner to take immediate administrative action with regard to such adjustments.

After a careful study of the question in the light of the briefs filed herein, we are now of the opinion that whether there is a net operating loss of petitioner for the taxable year 1944 and the amount thereof available as a carry-back to 1942 are issues in this proceeding and must be decided herein.

Petitioner is entitled to deduct from gross income a "net operating loss deduction computed under section 122." Section 23 (s), Internal Revenue Code, as added by section 211 (a), Revenue Act of 1939. Before 1942 the net operating loss deduction included "the amount of the net operating loss carry-over \* \* \*" from the two preceding years. It has never been questioned that with regard to a net oper-

ating loss carry-over from a preceding year, the existence and amount thereof is properly an issue in a proceeding involving a deficiency determined as to a later taxable year in which a taxpayer claims such carry-over under section 122. See *Moore, Inc.*, 4 T. C. 404, affirmed 151 Fed. (2d) 527; *Bush Terminal Building Co.*, 7 T. C. 793, 817; *Walter G. Morley*, 8 T. C. 904, 916. By the Revenue Act of 1942, the net operating loss deduction was made to include net operating loss carry-backs. Section 122 (b), Internal Revenue Code, as amended by section 153 (a) and (c) of the Revenue Act of 1942. The legislative history of this amendment indicates that Congress recognized that, in the usual case, a taxpayer could not determine the amount of the carry-back until the close of the future taxable year in which it sustained the net operating loss, and therefore would have to pay its tax without regard to that deduction, and later file a claim for refund. See Senate Report No. 1631, 77th Congress, 2nd Session, p. 123, C. B. 1942-2, p. 597.

In 1945 subsection 322 (g) was added to the Internal Revenue Code and made retroactive to 1941. That subsection reads as follows:

(g) Overpayments Attributable to Net Operating Loss Carry-Backs and Unused Excess Profits Credit Carry-Backs.—If the allowance of a credit or refund of an overpayment of tax attributable to a net operating loss carry-back or to an unused excess profits credit carry-back is otherwise prevented by the operation of any law or rule of law other than section 3761, relating to compromise, such



credit or refund may be allowed or made, if claim therefor is filed within the period provided in subsection (b) (6). If the allowance of an application, credit or refund of a decrease in tax determined under section 3780 (b) is otherwise prevented by the operation of any law or rule of law other than section 3761, such application, credit or refund may be allowed or made if application for a tentative carry-back adjustment is made within the period provided in section 3780 (a). In the case of any such claim for credit or refund of any such application for a tentative carry-back adjustment the determination by any court, including The Tax Court of the United States, in any proceeding in which the decision of the court has become final, shall be conclusive except with respect to the net operating loss deduction and the unused excess profits credit adjustment and the effect of such deduction or adjustment, to the extent that such deduction or adjustment is affected by a carry-back which was not in issue in such proceeding.

The report of the House Committee with regard to this subsection states in part as follows (House Report No. 849, 79th Cong., 1st Sess., pp. 31-32, reported in C. B. 1945 at p. 587):

In further recognition of the fact that the events which result in a net operating loss carry-back or an unused excess profits credit carry-back may not occur until a number of years after the close of the taxable year of the overpayment, subsection (d) of section 5 of the bill adds a new subsection (g) to section 322 of the Code. \* \* \* Section 322 (c) of the

Code in effect provides that where a taxpayer has filed a petition with The Tax Court for a redetermination of a tax for a taxable year, no credit or refund of an overpayment of such tax for such year, except as determined by The Tax Court and with certain other limited exceptions, may be allowed or made. However, under the proposed subsection (g) of section 322 of the Code, even though the tax liability for a given taxable year, for example, has already been litigated before The Tax Court, credit or refund of an overpayment attributable to a carry-back may be allowed and made, if claim for credit or refund is filed within the period prescribed in section 322 (b) (6), or if an application for a tentative carry-back adjustment is filed within the period prescribed in section 3780 (a). \* \* \*

Though it is the purpose of subsection (g) to permit taxpayers to receive credit or refund of an overpayment of tax resulting from a carry-back, even though such credit or refund normally would be barred by the doctrine of *res judicata* or by some other law or rule of law, it is not intended that any determination of issues, including carry-back issues, made by any court in a proceeding in which the decision has become final shall be open for reconsideration. Subsection (g) provides that in the case of a claim for credit or refund of an overpayment attributable to a carry-back, or in the case of an application for a tentative carry-back adjustment, the determination of any court, including The Tax Court, in any proceeding in which the decision of the court has become final, shall be conclusive except

with respect to the net operating loss deduction and the unused excess profits credit adjustment, and the effect of such deduction and adjustment, to the extent that such deduction or adjustment is affected by a carry-back which was not in issue in such proceeding. \* \* \* [Underscoring supplied.]

At the time of the Congressional enactment of all of the statutory provisions above referred to, section 272 (e) of the Internal Revenue Code provided that "The Board [of Tax Appeals] shall have jurisdiction to redetermine the correct amount of deficiency \* \* \*," and section 272 (g) provided as follows:

(g) Jurisdiction Over Other Taxable Years.—The Board in redetermining a deficiency in respect of any taxable year shall consider such facts with relation to the taxes for other taxable years as may be necessary correctly to redetermine the amount of such deficiency, but in so doing shall have no jurisdiction to determine whether or not the tax for any other taxable year has been overpaid or underpaid.

No change or amendment to these subsections of section 272 are made, or purported to be made, by the statutes dealing with carry-backs.

In the instant proceeding the determination of deficiency as to the taxable year 1942 was made on April 30, 1945, and the original petition was filed on July 13, 1945. At those times petitioner's return for the year ended September 30, 1944, had been prepared and filed. Petitioner was then in a position to know and claim its right to an operating net loss deduction arising from a carry-back of its net operating loss for 1944 in the determination of its cor-

rest tax liability for its taxable year 1942. It could have also filed a claim for credit or refund on account of such reduction. The record does not show whether any such claim was filed. It does show, however, that it raised as an issue in this proceeding its right to a deduction in the taxable year 1942 on account of losses alleged to have been sustained in 1944, which can only be construed as an issue involving its right to a net operating loss deduction in 1942 arising from net operating losses in 1944 to which it was entitled as a carry-back under the provisions of section 122(b).

It is our conclusion that this issue is properly before us in this proceeding under the provisions of section 272 (e) and (g), and consequently, we must decide in this case whether petitioner sustained a net operating loss in 1944 and the amount thereof. See *Acampo Winery & Distilleries, Inc.*, 7 T. C. 629; *Weir Long Leaf Lumber Co.*, 9 T. C. 990.

With regard to petitioner's contention that the matter of its deficiency determined for 1942 to be held open "until the Commissioner's determination of the existence or nonexistence of such operating loss [for 1944] shall have become final, or shall have become lost by the running of the statute of limitations," there is no precedent for the procedure suggested by petitioner; and, in addition, no practical reason exists for inaugurating such a procedure. In the absence of some statutory provision similar to section 3780, Internal Revenue Code, above referred to, there is nothing to require respondent, in considering petitioner's tax liability for its fiscal year



1944 as disclosed by its return, to do more than determine whether petitioner had taxable income for that year. If he is satisfied that petitioner had no taxable income, the respondent is not required to make a determination of the existence or amount of petitioner's operating loss for that year. Only with regard to petitioner's tax liability for prior or subsequent years would such a determination be required, for the purpose of ascertaining net operating loss carry-backs or carry-overs. Therefore, as a practical matter, no useful purpose would be served by holding open the question of petitioner's correct tax liability for 1942 until respondent does something which he is not required to do.

Upon the proof contained in the record before us, we are unable to find the existence or amount of any net operating loss of petitioner in its fiscal year 1944 which would give rise to a net operating loss deduction in 1942, the year before us. *H. B. Moore*, 8 B.T.A. 749, 754.

However, because of the novelty of the procedural problems presented, the intimation by respondent's counsel that some adjustment or agreement might be made administratively with regard to the net operating loss carry-back claimed by petitioner, the grave consequences to petitioner of a conclusive determination in this case, evidently unanticipated by it, of any rights incident to its alleged net operating loss carry-back from 1944, and the fact that the Court did not direct petitioner to proceed at the hearing herein with its proof as to existence and amount of such loss carry-back, we feel that a some-

what unusual procedure should be followed in the disposition of this case in order to accomplish a fair and equitable result.

The parties will be given sixty days after the entering of this Opinion within which to submit an agreed computation of the correct tax liability of petitioner for its fiscal year 1942, or to otherwise move in regard thereto.

If, within that period, no such computation is submitted or no motion is filed by either party, then, pursuant to our Opinion that the existence and amount of petitioner's alleged net operating loss carry-back from 1944 is properly here at issue and have not been proved by the evidence submitted,

Decision will be entered for the respondent.

Entered Mar. 24, 1948.

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[Title of Tax Court and Cause.]

### MOTION TO REOPEN CASE

Pursuant to Memorandum of Opinion herein, dated March 24, 1948, petitioner hereby respectfully moves that this case be reopened and set for trial upon the issue as to whether petitioner suffered a net operating loss for the taxable year 1944 as alleged in the Petition herein and as stated in the report of Internal Revenue in Charge, dated January 23, 1947, admitted in evidence as Petitioner's Exhibit 1 herein, and as to whether Petitioner is entitled to carry-back such loss to the year 1942.

Dated: May 17, 1948.

/s/ GEORGE ACRET,  
Attorney for Petitioner.

Received and Filed T.C.U.S. May 21, 1948.

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[Title of Tax Court and Cause.]

### ORDER

Petitioner filed herein on May 21, 1948 its Motion asking that this case be reopened and set for trial upon the issue of whether petitioner sustained a net operating loss for the taxable year 1944 which is available to it as a carry-back to the taxable year 1942, and the amount thereof, if any. This motion was filed within the time granted in our Memorandum Opinion entered herein on March 24, 1948. Upon due consideration, it is

Ordered: that petitioner's said Motion be and it hereby is granted, and that this proceeding be and it hereby is reopened for the purpose of hearing evidence upon the issue above stated; and it is further

Ordered: that this proceeding be set for trial upon the issue above stated at the first Los Angeles calendar to be had after July 1, 1948.

[Seal] /s/ JOHN W. KERN,  
Judge.

Washington, D. C.

May 26, 1948.

Served May 26, 1948.

THE TAX COURT OF THE UNITED STATES

Docket No. 8720

BIRCH RANCH AND OIL COMPANY,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

October 11, 1948—10:00 a.m.

(Met pursuant to notice.)

Before: HONORABLE C. R. ARUNDELL,  
Judge.

Appearances:

G. ACRET,

1210 Quinby Building,  
Los Angeles, California, appearing  
for the Petitioner.

E. C. CROUTER,

Honorable Charles Oliphant, Chief  
Counsel, Bureau of Internal Revenue,  
appearing for the Respondent.

PROCEEDINGS

The Clerk: Docket No. 8720, The Birch Ranch  
and Oil Company.

Mr. Acret: George Acret for the Petitioner.



There is a motion for continuance in the matter which I understand will not be opposed, and it is on a legitimate ground, I believe; that is the fact that the issues have been changed since the previous partial hearing of this matter and the issues now are not joined, and both counsel and I feel that there should be an amended complaint so that I can get at the matter properly and possibly enter into certain stipulations that will shorten the time of trial.

Mr. Crouter: E. C. Crouter for the Respondent, if the Court please. With respect to this case, if your Honor please, I would like just to be allowed to make a short review of its present status. The case is on this hearing calendar for a rehearing or further hearing. It was submitted once before, and I believe the Court held that the question of carry-back loss—the only year open now is 1942, and there is a question of a carry-back net operating loss from 1944 back to the taxable year 1942 involved here. There is some uncertainty as to the pleadings. I might point out that the memorandum findings of fact on the testimony previously entered was dated March 24, 1948, and to date there has been no amended petition. However, I can concede that an amended petition here specifically setting [3\*] forth the taxpayer's position would undoubtedly be helpful in the further hearing and presentation of the case, and for those reasons I have no objection to the continuance, but I would like to have a time placed on it so that we can have this case at issue

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\* Page numbering appearing at top of page of original Transcript of Record.

and have it presented sometime in the fairly near future.

Mr. Acret: We would ask leave to file an amendment to the petition within thirty days, and we would be ready for trial at any time after counsel have an opportunity to answer that amendment.

Mr. Crouter: That seems reasonable to me.

The Court: I don't quite know what happened in this case. I see an opinion here by Judge Kern. Did he set the case down for further hearing, or what?

Mr. Acret: I might supplement counsel's remark, your Honor. The part that was heard with respect to this case was the question whether or not this Court had jurisdiction in a matter concerning a deficiency for 1942 to determine on the merits the question of a net operating loss in the year 1944. The Court took that question under submission, and found it to be an unusual procedural question and held that the Court did have jurisdiction to determine the question of the 1944 net operating loss. However, since that hearing there has been a reaudit of the taxpayer's books and a thirty day letter filed by the agent in charge, which changes the issues. There has been a question in my mind that the thirty day letter is not [4] final, and for that reason up to this time we have not filed an amendment to the petition. I think counsel will stipulate with me that that thirty day letter as filed is final, and if so we can file our amendment and join issues. The situation is that the issues were changed during the pendency of this action, and we have not had opportunity to reframe them.

Mr. Crouter: If your Honor please, I would not

go along with counsel in what he was stating. It seems to me that a lot of that bears on the merits of the case. To answer the question your Honor asked, the opinion entered March 24, 1948, provided that decision would be entered, provided that within a designated time neither party submitted a motion for further proceedings. Now, the Petitioner about May 21, 1948 did submit a motion for further proceedings with respect to the net operating loss question and that motion was granted, so that that in effect has provided for further proceedings in the case merely as to the net operating loss carry-back question.

The Court: Well, isn't that more or less of a mathematical problem?

Mr. Acet: No, your Honor. It is a very complicated question and involves the fact that it is a reorganization of a reclamation district. The matter has been litigated and I believe there is no issue about what Judge Turner found with regard to the organization of the reclamation district, but counsel has re-raised the issue, and unless there would [5] be some stipulation of facts, there is an enormous amount of evidence to be presented concerning the organization of that district, which ultimately involves our right to make the deduction for payment of interest on the reclamation bonds. It is a \$120,000 deduction. If we were allowed to make that deduction we would suffer a net operating loss we have the right to carry back.

The Court: Well, will that case come up in the regular order covering the year 1944?

Mr. Crouter: No, if you Honor please, because there is no deficiency determined for that year.

Mr. Acret: That is what makes the difficulty. There is no deficiency.

The Court: How are you going to get a final determination of it?

Mr. Crouter: Well, the Bureau has acted upon the matter since the last hearing, and the Petitioner has had a notice disallowing the loss contended for in 1944, so that the Bureau has taken a position and the Petitioner does not agree with it. I might also state for your Honor's understanding we have already worked out a settlement of the carry-back deduction in the matter of 1944, which is very similar, and in a similar issue to that which was involved in the years 1942 and 1941, and which was also involved in this prior case of 1941, and 1941 is out of it now. I might state that the Bureau has had the same difficulty [6] that was involved in the case decided by Judge Turner as to the years 1937 and 1939, but that case went off on an accounting basis, and this precise question has never been decided. That is our difficulty.

The Court: Well, as I understand it, we have to decide this case for the years September 30, 1941 to September 30, 1942. What you propose to do is to carry back a loss of 1944 and apply it in these earlier years, is that correct?

Mr. Crouter: To the year 1942. By this reply the Commissioner states there is no loss allowable as a carry-back. That is the Commissioner's last action.

The Court: What I am trying to find out is, are



we going to litigate in this 1942 proceeding, the 1944 proceeding, to determine whether there is a carry back?

Mr. Crouter: I believe it is necessary, and I believe that is the conclusion which Judge Kern reached after hearing this prior case, the prior proceedings rather in this same case.

Mr. Acret: Your Honor would have to read this opinion to see how he reached the decision, but there is no other way for the taxpayer to secure relief. To secure justice it is necessary. We raised the question in our petition. Since we filed that petition the agent in charge made a reaudit and filed a thirty day letter, that is, since the hearing of this case another audit was made and another thirty day letter has been filed, and it is the issues that are raised on that new letter that we [7] have not yet filed an amendment concerning, and which we now desire to do, and we could do that within thirty days, and then the matter could be tried on the merits in accordance with Judge Kern's decision.

Mr. Crouter: If your Honor please, I have a copy of the memorandum findings of fact and opinion previously rendered, and I believe the last three paragraphs will serve to help answer your Honor's question.

The Court: I think I have it.

Mr. Crouter: The last three paragraphs, as I have outlined them, do provide for further proceedings if counsel has requested, and it is for that reason that Respondent agrees to that procedure.

The Court: Is there any way for a taxpayer to

get the benefit of a net loss after the prior year has been determined?

Mr. Crouter: I believe there is, if your Honor please, if it is not put in issue in a pending docketed case. That was one of the difficulties here, the pleadings were a little bit indefinite, and Judge Kern finally, after going over the pleadings as I recall this, very squarely held that this net loss carry-back question is an issue in this case. It was not fully brought out in the pleadings, but a little bit obscure, and it is provided in the statute which is quoted in the opinion, if your Honor please, the last sentence of that [8] decision.

The Court: I understand that carry-back, but what I have in mind is, suppose that the year 1942 is litigated before us and we determine a deficiency. Now ordinarily that becomes final, in the absence of an appeal. Well, now, later on it develops that there is a carry-back. What happens?

Mr. Crouter: My understanding is this, if the carry-back question is not in issue in the proceeding, then under the statute and the procedure the case is subject to adjustment for a net loss carry-back. That sometimes happens in cases where we stipulate. We had no loss carry-back question involved on the original pleadings in this case, therefore the case fell within the last sentence of the statute which is 322 (g) of the Internal Revenue Code. I will read that if the Court thinks it would be helpful here.

The Court: I don't know, but it seems to me it is not a very orderly way of handling these matters.

Mr. Acret: There is another point involved

necessarily with this question. The question as to deficiency in 1942 has not yet been decided. That was not considered on the merits of whether or not, if they had a right to make a deduction in 1941 of \$120,000, whether or not they had a right to make it concerning the year 1942. Now, either of those questions is open for decision on the merits in this case, and the decision of either of them eliminates the deficiency. [8-A]

If this Court finds that the reclamation district is properly organized and that the taxpayer has the right to make that \$120,000 deduction for 1942, in either case the deficiency is wiped out, so your Honor's assumption that the 1942 deficiency had been decided on the merits, I think, is not the fact.

The Court: Well, I don't mean that it has been necessarily decided on the merits, but there was a determination by the Respondent for 1942, and you brought the proceedings here.

Mr. Acret: Yes.

The Court: And you could have raised anything on the merits that you saw fit. Well, if you didn't it is too bad, and now the case is decided and I would not think that the procedure should be to hold up a 1942 deficiency to see if some later year you might happen to get a loss that you could carry back.

Mr. Acret: That is the question.

The Court: If you do, it seems to me the revenue is going to be tied up for years in these cases just to see what the future may bring forth.

Mr. Acret: Of course, we don't enjoy having the

matter held up and drawing interest on it either, your Honor, but the question that your Honor is now suggesting is the question that was gone into in the previous hearing and which was decided [9] by Judge Kern, and I think is *res judicata* to that extent.

The Court: Well, I will let him worry with it then in the opinion. It seems to me that the matter should be disposed of, and I would suggest that you get your amended petition in within 10 days, and let's get it at issue so that we can get it on the November calendar.

Mr. Acret: It would be rather difficult to do that, your Honor.

The Court: Why so?

Mr. Acret: The present petition is I think a thirty or forty page printed petition, and the issues are quite substantially changed by this recent thirty day letter, and it would take longer than that if I went to work immediately on it. It took thirty days to prepare that first petition, and we attorneys have other work as well. It would be a rather difficult, if not impossible situation, to file amendment within 10 days.

The Court: What I had in mind is, you asked that this case be reopened in May. You have had since May, haven't you?

Mr. Acret: Yes, that is true, your Honor, but I have taken the position that this letter is the same situation we were in with reference to the first hearing; it is not the finality of review that Judge Kern refers to in his opinion and his decision at that time,



that the issue can't possibly be joined, and while he had this matter under consideration the [10] first thirty day letter has now been changed to another thirty day letter, and we are still in the same situation we were before at the time of the first hearing, there is no finality of review, but I think counsel and I now, knowing that situation, can meet that by treating that as a final decision of agent in charge and join issue on it, but it will take longer than ten days to do it intelligently and with sufficient care to do it properly, as far as the rights of my client are concerned. I would ask for thirty days, if your Honor please. My client is fully able to respond to any amount of tax, and we ourselves regret the loss of time on account of the interest that is running.

The Court: All right, I will allow you thirty days.

Mr. Acret: Thank you.

The Court: How much time do you have to have to answer it?

Mr. Crouter: Twenty days, I believe if counsel will give me a copy of the amended petition as soon as forwarded, why then even ten days from date of filing would be sufficient.

Mr. Acret: That is my practice, and I will be pleased to do so.

Mr. Crouter: Then we will probably have an early calendar in 1949 and might be able to get to it then.

The Court: Well, I will give you 15 days then, to answer.

Mr. Crouter: Thank you, your Honor.

(Whereupon the above-entitled matter was continued generally.)

Filed T.C.U.S. November 4, 1948. [11]

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[Title of Tax Court and Cause.]

SUPPLEMENT AND AMENDMENT  
TO PETITION

Comes now the petitioner Birch Ranch & Oil Company, a corporation, with leave of court first had and obtained, and for its Supplement and Amendment to its Petition herein, alleges as follows:

I.

That petitioner by reference hereby incorporates each and every statement and allegation contained in paragraphs I to V of its Petition on file herein.

II.

That in Docket No. 109993 in an action concerning this petitioner entitled Birch Ranch & Oil Company, Petitioner, vs. Commissioner of Internal Revenue, Respondent, the above entitled court filed Findings of Fact finding and determining that Reclamation District No. 2035 is a bona fide reclamation district of the State of California; that this petitioner is the owner of lands situated in such district; and that such lands are subject to an accrual of taxes in the sum of \$120,000 per year for payment of interest upon bonds in the total sum of \$2,000,000 covering such lands and the principal of

which bonds, including accruing interest thereon, constitute a lien upon such lands until paid; that such Findings of Fact are contained in the Findings of Fact and Opinion filed in such Docket No. 109993 on April 20, 1944, that such Findings of Fact by reference are hereby made a part hereof.

### III.

That subsequent to the filing of said Findings of Fact, and pursuant thereto, respondent made a re-audit of petitioner's income tax return for the fiscal year ending September 30, 1944 in which respondent found and determined that petitioner's books and records are kept on a cash basis and that petitioner paid in cash as taxes an assessment of \$221,610.87 to such Reclamation District No. 2035 during the said fiscal year to cover accrued interest upon such bonds for such year, and that such deduction is a proper item of deduction; that a copy of such report is hereto attached as petitioner's Exhibit "1," that in such report respondent found and determined that petitioner suffered a net loss of \$102,720.00 during such fiscal year ending September 30, 1944.

### IV.

That notwithstanding such determination of such net loss for such fiscal year, respondent did thereafter under date of December 8, 1947, file a Second Report with respect to petitioner's income tax return for such fiscal year in which report respondent disallowed such deduction of \$221,610.87; and that as a result of such disallowance of such deduction

determined that petitioner had a net income for such taxable year of \$34,711.50, such disallowance being made upon the ground stated in such report as follows:

“For the history of the taxpayer see prior Agent’s reports and U. S. Tax Court’s findings of fact and opinion in re: Birch Ranch & Oil Co. vs. Commissioner, Docket No. 109993.

“The additional Net loss as shown in this report is brought about by the allowance, in full, of amounts paid by the taxpayer in this fiscal year for assessment taxes on Reclamation District #2035. A part of the amount paid in this year covers amounts accrued on the corporation’s books in prior years, and disallowed in the prior Agent’s reports as deductions since the corporation was on a cash basis. For a breakdown of these amounts see Schedule 1-A of this report.”

that a copy of pages 1, 2 and 8 of such report are hereto attached as Exhibit “2” hereof.

#### V.

That with respect to the last named report, the respondent erred as follows: in disallowing said deduction in said sum of \$221,610.87; in holding that petitioner did not suffer such net loss of \$102,720.; in determining that Reclamation District No. 2035 is not a bona fide political subdivision of the State of California; in holding that the interest accruing thereon does not constitute a bona fide lien against petitioner’s land until paid and that such assessment taxes, when paid, are not properly deductible as assessment taxes paid.



## VI.

That petitioner in fact paid assessment taxes to the Treasurer of Yolo County, California, to cover interest of such bonds accruing as a lien against petitioner's land for such current year, as stated in respondents' said report dated January 23, 1947, as follows:

the Treasurer of Yolo County, California.....	\$123,516.10
the Treasurer of Yolo County California .....	\$123,516.10
Less: Amounts previously paid .....	(5,394.72)
Plus: Amount not previously accrued on books, but paid in current year on old Calls .....	769.49*
Total.....	<u>\$118,890.87</u>

Amounts allowed in this report consist of four payments in this year, by Certified Checks as follows:

(1) Check No. 28553 Dated 12/29/43 .....	\$ 64,422.51
(2) Check No. 29537 Dated 6/28/44 .....	59,093.59
(3) Check No. 20778 Dated 8/12/44 .....	37,325.28
(4) Check No. 618 Dated 9/20/44 .....	60,769.49*
Total.....	<u>\$221,610.87''</u>

## VII.

That petitioner in fact suffered an operating loss for such fiscal year in said sum of \$102,720 as established by respondents' such report dated January 23, 1947.

## VIII.

That petitioner by reference hereby incorporates Opinion of the Honorable John W. Kern filed herein in June 30, 1947, as part of this Supplement and Amendment.

Wherefore, petitioner prays that it have relief as prayed in its petition herein with respect to its fiscal year ending September 30, 1942, and that in addi-

tion, in the event this Court should deny petitioner any part of such relief as prayed for in such petition with respect to the said year ending September 30, 1942, that petitioner be adjudged entitled to carry back such part of such operating loss for such fiscal year ending September 30, 1944, as may be necessary to off-set any part of any deficiency involving such fiscal year ending September 30, 1942.

/s/ GEORGE ACRET,

Attorney for Petitioner.

Received and Filed T. C. U. S. November 12, 1948.

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[Title of Tax Court and Cause.]

ANSWER TO PETITIONER'S SUPPLEMENT  
AND AMENDMENT TO PETITION

The Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, for answer to the Supplement and Amendment to Petition heretofore filed in this proceeding, admits and denies as follows:

I.

In response to the allegations contained in paragraph I of the Supplement and Amendment to Petition, the respondent relies upon and hereby incorporates by reference the allegations contained in paragraphs I through VI and all sub-divisions thereof in the respondent's answer previously filed on or about August 29, 1945.

## II and III.

The respondent denies the allegations contained in paragraphs II and III of the Supplement and Amendment to Petition.

## IV.

Admits that the respondent has made a determination of a disallowance of a deduction claimed by the petitioner for the taxable year 1944 in the amount of \$221,610.87 for alleged taxes or interest paid, and that as a result of such disallowance the respondent has found and determined that petitioner had no net loss carry-back from 1944 to the taxable year 1942; admits that a copy of pages 1, 2 and 8 of the last report, of December 8, 1947, is attached to the Amendment to Petition; and the respondent denies the remaining allegations of paragraph IV of the Supplement and Amendment to Petition.

## V.

The respondent denies the allegations of error contained in paragraph V of the Supplement and Amendment to Petition.

## VI and VII.

The respondent denies the allegations contained in paragraphs VI and VII of the Supplement and Amendment to Petition.

## VIII.

The reference in paragraph VIII of the Supplement and Amendment to Petition to the prior opinion of the Honorable John W. Kern, filed herein on

March 24, 1948, under the Court's rules, apparently requires no admission or denial by the respondent.

IX.

The respondent further denies that the petitioner is entitled to any deduction for interest or taxes paid during 1942 and 1944 and alleges that it is not entitled to any net-loss carry-back from the year 1944 to the year 1942, on account of payment of any interest or taxes during 1944, under any of the provisions of Section 122 of the Internal Revenue Code.

Wherefore, it is prayed that the respondent's determination of deficiencies for the taxable year 1941 and 1942 be sustained and approved, and that the petitioner's alleged net-loss carry-back from the taxable year 1944 to the taxable year 1942 be denied.

/s/ CHARLES OLIPHANT,

ECC,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel.

E. C. CROUTER,

Special Attorney,

Bureau of Internal Revenue.

Received and Filed T.C.U.S. December 1, 1948.



[Title of Tax Court and Cause]

### STIPULATION OF FACTS

It is hereby stipulated and agreed, by and between the parties hereto, by their respective counsel, that the following facts may be taken as true, without prejudice to the right of either party to introduce other and further evidence not inconsistent therewith, and subject to the exception stated at pages 15-16, below:

1. The petitioner is a Nevada corporation, with its principal office in Los Angeles, California. Its income tax returns for the years involved herein were filed with the Collector of Internal Revenue in that city.

2. The Menges Oil Company, a corporation, was the owner of partially developed oil lands in the Brea Oil Field, in Orange County, California. The stock of the corporation was owned by A. Otis Birch, his wife, M. Estele C. Birch, B. F. Conaway, his wife, Anna M. Conaway, Louise Smith and her sister, Ruth Smith. The Conaways were the parents of Mrs. Birch, and the Smith sisters were the nieces of Birch. Louise Smith married C. Harold Hopkins, and Ruth his brother, J. J. Hopkins. They are commonly referred to in this proceedings as the Hopkins sisters. Birch and his wife and Conaway and his wife owned in equal amounts 70-17/18 per cent of the stock of the Menges Oil Company and the Hopkins sisters similarly owned the balance of 29-1/8 per cent. The Menges Oil Company was dis-

solved in September 1911, and its assets were transferred to a partnership known as Birch Oil Company. The stockholders of the Menges Oil Company became partners in the Birch Oil Company and their interests in the partnership were in the same proportions as their stock ownership in the corporation had been.

3. In 1914 Birch Oil Company purchased about 13,000 acres of overflow lands situated about five miles from Sacramento, in Yolo County, California, and in the Sacramento River Valley. The lands were purchased for use in farming and stock raising, and came to be known as the Conaway Ranch. Additional acreage was thereafter purchased and by 1918 the ranch contained about 20,000 acres. All purchases had been made at \$35 per acre.

4. At the time of the original purchase in 1914, the Sacramento and San Joaquin Drainage District, created under the laws of California, had started a flood control project in Sacramento River Valley. The project called for the acquisition of a by-pass, known herein as Yolo By-pass, across the Conaway Ranch, for the passage of excess floodwaters of the Sacramento River and its tributaries.

5. In 1914, when Birch Oil Company purchased the first of the lands comprising the Conaway Ranch, the by-pass was being surveyed, and it was expected that about one-half of the ranch would be taken for that purpose. The Reclamation Board of the State of California informed Birch Oil Company that if it would construct a levee across its

ranch property, adjacent to the by-pass, an assessment would be made against all the lands in the Sacramento and San Joaquin Drainage District to pay Birch Oil Company for flowage rights through the by-pass and for the construction of the levee. Birch Oil Company expected to receive \$25 an acre for the acreage used for the by-pass. Such acreage, according to law, could not be fully reclaimed and was suitable for grazing only.

6. Desiring to reclaim and develop the lands comprising the Conaway Ranch, the Birch Oil Company, in 1918, filed a petition with the Board of Supervisors of Yolo County, California, for the creation of a reclamation district which would include 24,210 acres and would cover the whole of the Conaway Ranch and twenty-odd other parcels of land not owned by the Birch Oil Company or its members. In April 1919, the establishment of Reclamation District No. 2035, comprising approximately 21,000 acres, was approved by the Board of Supervisors. Excluded from the district as approved were some 1,300 acres of the Conaway Ranch and all except eight of the twenty-odd other parcels of land not owned by the Birch Oil Company or its members.

7. Organization of the district was completed and the County Board of Supervisors appointed Conaway, C. Harold Hopkins, and a man named Armfield as trustees for the district. In June 1919, the trustees employed an engineer and directed him to prepare plans for the reclamation and irrigation of lands in the district, with estimates of the cost of

the necessary improvements. In June, 1920, the trustees approved the plans submitted by the engineer and his estimate of \$2,264,740 as the cost of the improvements. The plans submitted called for the construction of the main levee along the edge of the Yolo By-pass, as above described. The plans were approved by the Reclamation Board of the State of California in October 1920, and in December of the same year, by the Board of Supervisors. Commissioners of assessment were appointed to assess the value of the benefits to the lands in the district from the improvements contemplated and to apportion the cost of said improvements according to the benefits that would accrue to each tract of land in the district. Thereafter, and prior to July 2, 1924, the commissioners made the assessment and apportionment for which they were appointed. The assessment was approved by the Board of Supervisors on July 23, 1924, and the list of assessment was filed on the same day with the County Treasurer of Yolo County.

8. The Birch Oil Company, under the direction of the district's engineer, built the improvements called for in the reclamation plan and financed all the costs, which were slightly in excess of two million dollars. The work was substantially completed by 1925, at which time the improvements consisted of 45 miles of roadways, 47 miles of irrigation canals, 55 miles of drainage canals and ditches, and included bridges, pumping plants and other structures necessary for the development of the lands in



the district. By 1925 Birch had acquired individually and at undisclosed costs seven of the eight parcels of land which with the Conaway Ranch comprised the land of the district. The parcel not so purchased consisted of 240 acres.

9. In the meantime, the Hopkins sisters, being desirous of disposing of their interests in the Conaway Ranch, by agreements dated January 1, 1924, sold such interests to Birch and Mrs. Birch for \$787,000, an amount designed to pay them their proportionate part of the Birch Oil Company funds invested in the ranch. Under the agreements each of the sisters agreed to accept bonds of Reclamation District No. 2035 in the principal amount of \$393,000 and cash in the sum of \$500. Birch and his wife agreed to cause the district to issue bonds in an amount of at least \$800,000, which were to constitute a prior lien on all of the property in the district, and further promised to deliver on or before February 1, 1925, to each of the sisters the amount of the bonds and cash called for by the agreements. Birch and his wife were to have immediate and absolute possession and control of the properties acquired from the Hopkins sisters and were to be entitled to all rents and profits of every kind therefrom and were to assume all liabilities and burdens incident to the ownership thereof. The bonds not having been issued at the time of the agreements on January 1, 1924, Birch gave to each of the sisters his promissory note in an amount equal to the amount of the bonds she was entitled to receive under the agree-

ments. The notes were to run for 10 years and were to draw interest at 6 per cent per annum from January 1, 1924, for a period of 5 years, and at 7 per cent thereafter. Birch had the option of paying the notes in full at any time prior to the expiration of the 10 year period.

10. According to the minutes, the landowners, at an election held on August 28, 1924, voted to issue bonds to pay for the reclamation work which had been done, and on October 26, 1924, the trustees adopted resolutions providing for the issuance of the bonds.

11. On January 5, 1925, the trustees of the district adopted resolutions directing that the district pay Birch and Conaway \$2,000,000 for moneys advanced in the construction of the improvements; that Warrant No. 1 of the district be issued to them in that amount; that the bonds of the district be placed in the hands of the County Treasurer; and that the County Treasurer be requested to advertise the bonds for sale at the earliest possible date. On the same day Warrant No. 1 for \$2,000,000, drawn on the Treasurer of Yolo County, was issued to Conaway and Birch. The warrant was approved by the Board of Supervisors of Yolo County and was presented for payment to the County Treasurer but was not paid for want of funds.

12. On January 7, 1925, the trustees of the district delivered to the County Treasurer bonds of the district totaling \$2,264,740. The bonds were dated January 1, 1925, and bore interest at the rate of 6 per cent per annum until paid. They were in denom-

inations of \$1,000. The first \$227,000 thereof were to mature on January 1, 1935, with a like amount maturing on January 1 of each year following until January 1, 1944, when the bonds then remaining and amounting to \$221,740, were to mature. Also on January 7, 1925, the County Treasurer gave notice that on January 23, 1925, he would sell Bonds Nos. 1 to 2,000, inclusive, of \$2,000,000 par value, to the highest bidder, and stated that outstanding warrants of the district, with accrued interest thereon, would be accepted in payment for the bonds. Birch, acting for himself, Mrs. Birch and the Conaways, was the highest bidder, his bid being \$2,000,000 plus accrued interest. Being the highest bidder, he became the purchaser of the bonds and gave in payment therefor Warrant No. 1 of the district, which had been received by him and Conaway in payment for the building of the improvements for the district.

13. Upon receipt of the bonds of the district, Birch delivered to each of the Hopkins sisters \$393,000 par value of such bonds, or a total of \$786,000 pursuant to the agreements of January 1, 1924, whereunder he and his wife had acquired from the Hopkins sisters all of the interests of the latter in the Conaway Ranch. Upon delivery of the bonds, the Hopkins sisters delivered to Birch the promissory notes covering the purchase price of their interests in the ranch which had been received from him at the time of the January 1, 1924 agreements. At the same time they made formal conveyance to Birch and his wife of all their interests in the Conaway Ranch.

14. At or about the same time and pursuant to the terms of agreements dated January 10, 1925, the Hopkins sisters granted to Birch and his wife the right to purchase the bonds received by them as above set forth, at the prices and on the terms set forth in the said agreements. According to these agreements, Birch and his wife offered and agreed to purchase at face the bonds in question, the purchases from each sister to be made in installments of \$39,-300 on January 1, 1926, and on January 1 of each year thereafter until January 1, 1933, with a final installment of \$78,600 on January 1, 1934, and on each purchase date to buy all matured coupons appertaining to the bonds covered in the particular installment. At each installment date the sale of the bonds by the Hopkins sisters to Birch and his wife was to be completed at the option of the Hopkins sisters. To assure payment for the respective installments of the bonds, Birch and his wife agreed to deliver to B. F. Conaway and C. Harold Hopkins, as trustees, the balance of the district's outstanding bonds in the amount of \$1,214,000, and upon default in the payment of any of the above installments, the Hopkins sisters were to be permitted to sell, or have sold, so much of the bonds held in trust as should be required to pay the amount in default. The trustees might also release to Birch and his wife such of the bonds as might be required by them as a pledge for money borrowed to pay any current installment. Otherwise the bonds held in trust were to be released by the trustees only upon the written consent of the Hopkins sisters or upon full performance of the



agreements by Birch and his wife. In the event the Hopkins sisters should elect at any installment date not to sell the bonds called for by the agreements, Birch and his wife had the option to declare the agreement at an end. Provision was also made that Birch and his wife, on 90 days notice, might elect to buy bonds in advance of the regular installment dates provided and similarly might declare the entire agreement at an end if the Hopkins sisters should reject the offer. In respect of all purchases prior to January 1, 1929, Birch and his wife were to pay interest at the rate of six per cent, the rate called for by the bonds. On purchases after that date, they were obligated to pay seven per cent or one per cent over the interest provided for in the bonds.

15. In 1926 Birch entered into an agreement with the Conaways for the purchase of their interests in the ranch and in the bonds of Reclamation District No. 2035. The purchase price was paid in cash and in installments.

16. Beginning with January 1, 1926, the first installment date under the agreements of January 10, 1925, the Hopkins sisters elected to sell the bonds to Birch and his wife pursuant to the terms of the said agreements. Birch and his wife made the payments on the bond purchases as called for in the agreements and as elected by the Hopkins sisters until the early 1930's, when, due to the depression and a resulting lack of funds, they were unable to make the further payments on the dates prescribed, and extensions of time have thereafter been allowed.

The bonds paid for in the face amount of \$476,000 were delivered to Birch and his wife. The Hopkins sisters, in April, 1943\*, still held the remaining \$310,000 of the said bonds, but still held Birch and his wife liable on their obligations under the agreements of January 10, 1925. Their interest is in the receipt of the cash payments provided for in the contracts and they are unwilling to accept anything else. Of the \$476,000 par value of the bonds paid for by Birch and his wife and received from the Hopkins sisters, \$10,000 par value of such bonds were sold to Lula M. Minter and \$86,000 passed into the hands of the Great Republic Life Insurance Company, a corporation of which Birch was president. There was later a dispute between petitioner and the insurance company over rights of petitioner in and to the said bonds, the exact basis for which dispute is not shown.

17. On October 15, 1934, Birch and his wife organized Birch Ranch and Oil Company, the petitioner herein, and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000. Birch had been having difficulties during the depression years in

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\*On April 5 and 6, 1943, The Tax Court heard the case of Birch Ranch and Oil Company, Dkt. 109993, Mem. Op. entered Apr. 20, 1944, which related to the years 1937 and 1939.

borrowing on his personal credit the moneys needed for the operation of the ranch, and the petitioner was organized for the purpose of procuring needed bank credit.

18. Also on October 15, 1934, Birch and his wife organized a second Nevada corporation, to be known as Birch Securities Company. To that corporation they transferred \$1,594,000 par value of the bonds of Reclamation District No. 2035, being all of the bonds of the district except the \$310,000 still in the hands of the Hopkins sisters and those held by the insurance company and Lula M. Minter. Of the bonds so transferred, \$1,214,000 were transferred subject to the trust under the contract with the Hopkins sisters. In addition, they transferred to the Securities Company the corporate stocks referred to in the preceding paragraph. Birch Securities Company was organized as a holding company, and solely for the personal convenience of Birch. It engaged in no other business than that of a holding company.

19. Birch and his wife also organized on October 15, 1934, a corporation known as the Birch Holding Company, and transferred to it the stock of the petitioner and that of Birch Securities Company, which stock had been received by them for the assets transferred to such corporations. Birch received 49 per cent of the stock of the Holding Company, and his wife 51 per cent. Birch Holding Company was organized solely for the purpose of holding the stock of the petitioner and that of Birch Securities Company. It has not conducted any

other business. Birch became president of the three corporations. Mrs. Birch has left to him the determination of all matters pertaining to the administration of the affairs of the three corporations.

20. Beginning with 1937, and until April, 1943, no amount was paid in any year by the petitioner as interest on the \$1,594,000 of such bonds transferred by Birch and his wife to the Birch Securities Company, nor has it paid any amount as interest on the \$86,000 of such bonds held by the Great Republic Life Insurance Company. As to the bonds held by the insurance company, there was a dispute between that company and petitioner over petitioner's rights in and to those bonds. They were ultimately acquired by petitioner from the insurance company in 1940, for \$65,000. For each of the fiscal years 1937 and 1939 the petitioner did pay \$600 to Lula M. Minter as interest on the \$10,000 par value of Reclamation District No. 2035 bonds which had been acquired by her. It also paid in each of those years \$18,600 to the Hopkins sisters, that amount being six per cent on \$310,000, which was the amount still owing by Birch and his wife to the said sisters under the agreements of January 10, 1925, and was likewise the face amount of reclamation district bonds still in the hands of the Hopkins sisters.

21. On its books for the fiscal years 1937 and 1939, the taxable years herein, the petitioner accrued \$120,000, to represent interest on the entire \$2,000,000 par value of issued bonds of Reclamation District No. 2035. For the fiscal year 1937, it entered the



\$18,600 paid to the Hopkins sisters, as above stated, as a loan to Birch Securities Company. Birch Securities Company, on its books, treated the receipt of the \$18,600 as a loan from petitioner and charged a net of \$17,382.75 as interest paid to the Hopkins sisters. It claimed a deduction on its income tax return for that year in the latter amount.

22. At no time has any amount been paid into Reclamation District No. 2035, or set aside by Birch and his wife or the petitioner, for the purpose of paying off the bonds of the district, even though the bonds began to mature on January 1, 1935, at the rate of \$227,000 per year.

23. Since its organization the petitioner has operated the Conaway Ranch, devoting it to the growing of crops and the raising of sheep. The petitioner, as owner of the Company Ranch, has borne all of the costs and expenses of maintaining and operating the improvements of Reclamation District No. 2035 and treats such costs as a part of its expenses in operating the ranch, all in a manner which would be no different if there were no reclamation district, whether formal or actual. The district has no expense not taken care of by the petitioner.

24. All crops grown on the ranch during a given fiscal year were sold in the same year in which grown. The herd of sheep was kept at an average of 3,500, with losses being replaced by younger animals. All sales were made for cash, as were all purchases. The petitioner kept a separate set of books with respect to the ranch operations, during the fiscal

years 1937 and 1939. The ranch books were kept on a cash basis. For each of such taxable years Form 1040 F was used in reporting income from the operations of the ranch, and reported the income or loss therefrom on a cash basis.

25. Provided, however, that the respondent, in this proceeding, relating to Docket No. 8720, does not by anything contained herein stipulate or agree that there were issued or outstanding at any time, under any State or Federal laws, any valid or lawfully issued bonds of Reclamation District No. 2035, which were owned or held by A. Otis Birch, or Mrs. A. Otis Birch, or any corporation owned in whole or in part or controlled by them, including the petitioner corporation, or that the petitioner was under any legal liability to pay any "call" or "assessment" for the payment of any amounts of "interest" or "taxes" for which deductions are claimed for Federal tax purposes, and the respondent does not admit that the petitioner did at any time pay any such interest or taxes which constitute allowable tax deductions.

/s/ GEORGE ACRET,  
Counsel for Petitioner.

/s/ CHARLES OLIPHANT,  
ECC.

Chief Counsel, Bureau of Internal Revenue, Counsel  
for Respondent.

Filed T.C.U.S. February 11, 1949.

[Title of Tax Court and Cause.]

ANSWER TO SECOND SUPPLEMENT AND  
AMENDMENT TO PETITION

Comes Now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the second supplement and amendment to petition filed in this proceeding on February 11, 1949, alleges as follows:

II.

Denies the allegations contained in the second supplement and amendment to petition, paragraph II, page 2.

IX.

Denies the allegations contained in paragraph IX of the second supplement and amendment to petition.

X.

Denies each and every allegation contained in the second supplement and amendment to petition not hereinbefore specifically denied.

Wherefore, it is prayed that the determination of the Commissioner of Internal Revenue be approved.

/s/ CHARLES OLIPHANT,

ECC.

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

E. C. CROUTER,  
Special Attorney,  
Bureau of Internal Revenue.

Filed T.C.U.S. February 15, 1949.

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The Tax Court of the United States

Docket No. 8720

BIRCH RANCH & OIL COMPANY,  
a corporation,

Petitioner.

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

(Met pursuant to notice.)

Before: Honorable Luther A. Johnson,  
Judge.

Appearances:

GEORGE ACRET,

1210 Quinby Building,  
650 South Grand Avenue,  
Los Angeles, California,

Appearing for the Petitioner.



EARL C. CROUTER,

(Honorable Charles Oliphant,  
Chief Counsel, Bureau of Internal  
Revenue),

Appearing for the Respondent.

### PROCEEDINGS

The Court: The Clerk will call the next case, please.

The Clerk: Docket No. 8720, Birch Ranch & Oil Company.

Mr. Crouter: Ready for the Respondent.

Mr. Acret: Ready for the Petitioner.

The Court: The appearances have been noted, and are Earl Crouter for Respondent and George Acret for the Petitioner.

This case bears rather an old docket number. Hasn't there been some proceedings in this case before?

Mr. Acret: Yes, your Honor. There is a situation here, and it may be of help to the Court if I would make some statements.

Mr. Crouter: If your Honor please, before we proceed with any portion of the hearing, Respondent at this point moves that all witnesses who may be available now or come later be excluded from the hearing room. That is for reasons which I will be glad to explain or argue, if necessary.

The Court: Are there any witnesses in the court room now?

Mr. Acret: Mr. Birch is here, the president of

the Petitioner corporation; Mr. Landrum, the secretary is here. It is my understanding the parties to an action have a right to be present—— [3\*]

The Court: Yes.

Mr. Acret: ——as a matter of their interest in the case. However, I don't know, other than their wanting to hear what is going on, I don't know of any reason why they shouldn't be here.

The Court: Do you want them to leave the court room now?

Mr. Crouter: I believe the rule should be invoked at the commencement.

The Court: Any witnesses now in the court room, if they will come forward now, the Clerk will administer the oaths to the witnesses.

Mr. Acret: Mr. Birch and Mr. Landrum.

The Court: Mr. Birch and Mr. Landrum will be sworn now. There are no other witnesses in the court room, as I understand it. The rule having been invoked, the witnesses other than the Petitioner of the case will retire from the court room and not discuss the case or be permitted to discuss it.

Mr. Acret: That means, Mr. Landrum, you are required to wait outside the court room because we can only have one representative of the corporation.

Your Honor, because I believe it would be of some assistance to the Court in a case of this character, I have prepared Petitioner's Trial Memorandum of Points and [4] Authorities, if your Honor would like to have it.

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\* Page numbering stamped at top of page of original Reporter's Transcript.

The Court: I believe it might be well. The Court is entirely unfamiliar with what the issues are. It might be well for counsel of Petitioner to state the nature of the case, the issues involved, and also give the Court the benefit of any information as to what has transpired before in this case.

Mr. Acret: Your Honor, has the Court had an opportunity to read the petition and the amendment to the petition?

The Court: No, the Court is entirely unfamiliar. All he knows is the title of the case.

Mr. Acret: Very well. The petition involved has a sufficient number of ultimate facts that we thought it would be of advantage to have it printed. Your Honor will find it is a printed petition.

The Court: What are the taxable years?

### OPENING STATEMENT ON BEHALF OF THE PETITIONER

By Mr. Acret:

The taxable years involved are 1941 and 1943, originally in the petition, and by reason of the facts that I am about to relate, by reason of action taken by the Commissioner, the issues have changed so that the years involved, strange to relate, and your Honor may be astonished to hear it, first, is the year 1944. It is the Petitioner's [5] right to carry back a loss in 1944, to wipe out the deficiency assessment involved herein for 1943, and the case has a considerable background.

The Court: The Court would like to hear the background.

Mr. Acret: Yes, your Honor. Judge Turner heard a proceeding, Docket No. 109,993, many years ago; 1942, or something like that, involving the principal issues that are involved here, that is, the validity of the creation of a reclamation district in Yolo County, in this State. That is just north of Sacramento, and including the validity of \$2,000,000.00 of reclamation bonds of this Reclamation District 2035, and involving this Petitioner's right to make a deduction of \$120,000.00 a year for payment of amount into the County Treasury sufficient to meet 6 per cent interest on that \$2,000,000.00 of bonds.

Judge Turner made rather voluminous findings of fact, and very accurate ones, in view of the short time of the hearing and the large number of facts which were involved.

The Court: Did that hearing before Judge Turner result in a decision being rendered by him upon that issue?

Mr. Acret: I was about to relate—no, your Honor, the case went on in another manner, that is, Judge Turner, though he made findings of fact in detail with reference to the organization of the District and the issuance [6] of the bonds and the incorporation of this Petitioner and the purposes for which it was incorporated, he decided the matter on a basis of accounting; that is, that the Petitioner was on a cash system of accounting, when, as to the items of deduction involved, they had only approved them;



hadn't paid them, and for that reason, however, he did allow as interest paid certain amounts of those years that the Petitioner had, in fact, paid.

Also, there was involved in that case, and I mention it now because it will have to do with my objection to the materiality of——

The Court: Where is Judge Turner's opinion recorded? Was it a memorandum of opinion or what?

Mr. Acet: It is a detailed opinion. Do you have the citation, Mr. Crouter? I don't have it at hand.

Mr. Crouter: That is a memorandum opinion. It is not a reported case. For the record at this point, we might just state that was in Docket No. ——

The Court: Give the docket number and about when it was.

Mr. Crouter: 109,993, Memorandum of Findings of Fact and Opinion entered April 20, 1944, and that related to the fiscal years ended September 30, 1937, and 1939.

Mr. Acet: That is right.

The Court: What was the next step taken in the case? [7]

Mr. Acet: I was about to call your Honor's attention to the fact in matters that have heretofore been heard in this, that opinion was admitted as Exhibit 2 in this proceeding, and your Honor will find the opinion in the file as Exhibit No. 2.

Now, the next step was that, while I think the matter was pending for decision before Judge Turner, the deficiency assessment that is involved for

1941 and 1943 was made, and this Petitioner filed its petition that is involved herein.

The Court: That is under the present docket number, is it?

Mr. Acet: Yes, your Honor. Then the next thing that happened is that for 1944, the Commissioner made an audit of the Petitioner's books, and filed a report which increased the loss which Petitioner had shown for 1944 from \$84,000.00 to \$186,000.00, and that in that report—and it is Exhibit No.—it is one of the exhibits in this proceeding—I believe it is Exhibit No. 1.

The Court: Those exhibits you refer to, are those attached to a stipulation of facts?

Mr. Acet: No, they are not, your Honor. They were just admitted in a manner I will relate as I come to it in its chronological order.

In that report, which I will refer to as the first [8] report, and it is attached as Exhibit 1 to our amendment to the petition herein, also, it is dated January 23, 1947, the agent in charge stated that "For the history of the taxpayer, see prior agent's report in U. S. Tax Court's findings of fact and opinion herein in Docket No. 109,993." That is the one we have just been talking about. It says, "The additional net loss, as shown in this report, is brought about by the allowance in full of amounts paid by the taxpayer in this fiscal year for assessment taxes on Reclamation District No. 2035. Part of the amount paid in this year covers amounts accrued on the corporation books in prior years, and was disallowed in the prior agent's report, and

deductions, since the corporation was on a cash basis."

Now, in the meantime, along about June, 1947, this matter came up for hearing in this court, before Judge Kern. When it did come up for hearing, as the attorney for the Petitioner, I then stated that in view of this report, we were adopting the contention that we were on a cash basis, and that if we were on a cash basis, that, therefore, the deficiencies that are involved in this proceeding for 1941 and 1943, our position was not well taken because we had only accrued those items and hadn't paid them. We put in evidence the exhibits with Judge Turner. He heard the matter and took it under advisement.

The Court: You mean, Judge Kern? [9]

Mr. Acret: Judge Kern, and took it under advisement, took under advisement the question of whether or not in a proceeding which only involved 1941 and 1943, if this Court had jurisdiction to hear anything concerning 1944, and the validity of that loss. In other words, the loss that was stated in this report that the agent in charge changed from eighty four thousand to a hundred and eighty-six thousand, and he filed, Judge Kern filed an opinion, holding that we were entitled, or that this Court did have jurisdiction to consider 1944, and that we would be entitled to carry back such loss as we might be able to establish.

The Court: What is the date of Judge Kern's opinion?

Mr. Acret: That is sometime in the fall of 1947,

if I remember correctly. Counsel apparently has it. It is the file, I presume.

The Court: All right.

Mr. Acret: Now, in the meantime, your Honor, relying on this first report and the fact we were held to be on a cash basis, the Petitioner paid the amount that is involved herein for 1941, because there was no possibility, there was no right to carry back a loss of '44 for more than two years, so we paid 1941, in the sum of twelve thousand odd dollars, but relying on the right to carry back the 1944, we filed this supplement and amendment to petition, which raises the issues that I am about to relate that are [10] involved here. That is the history leading up to——

The Court: Petitioner's counsel will state what the issues are at this time. Counsel is now ready to proceed for Petitioner concerning the issues now involved?

Mr. Acret: Yes, your Honor. After we made this payment of the 1941 assessment, the Commissioner then caused a reaudit of the Petitioner's books of 1944 to be made, and in that reaudit he disallowed this deduction of interest paid in 1944 to meet the assessment on the bonds, which wiped out the loss entirely for 1944, and that is on the theory that I am about to go into in detail, that this Reclamation District is not a bona fide district, nor the bonds, and that, so to speak, the matter of paying the taxes to the County Treasurer by the Birch Ranch & Oil Company, which owns the land in the District, to the Birch Securities Company, this peti-



tion is like taking the money from the right-hand pocket, so to speak, and putting it in the other.

The Court: In other words, we are now to pass on the Commissioner's disallowance of the payment of those funds, and the validity of those payments. Is that right?

Mr. Acret: Well, there is a little more to it than that, but we now come to the issues raised by this disallowance. This is like all complicated matters; it is capable of being made very clear and simple. It is just a quantity, rather than any difficulty concerning it, and [11] I would like to state at the outset, your Honor, that there isn't a single fact in this case that I think is controvertible or that we shouldn't be able to agree on. What the question of law is going to be, and I think your Honor will see that, even at the close of the opening statement, the question of law is going to be that where a reclamation district is organized by a group of landowners consisting of nine, and one of the landowners makes the improvements himself on a contract with the Reclamation District of a value of \$2,000,000.00, for that \$2,000,000.00 gets a reclamation district warrant in that amount, and where subsequently, after the formation of the district, and five years later, under the provisions of Section 3480 of the Political Code of California, which I will refer to hereafter as the Reclamation Act, those landowners, by a vote, under the provisions of the Act, voted to put a bond issue against the assessment, bond issue against the lands of the District, to pay the assessment of \$2,000,000.00 and where

Mr. Birch, who, with his wife, is the sole owner of this Petitioner and other corporations that I am about to relate, together with two associates of his at the time, traded in their warrant, as provided in law, for the whole \$2,000,000.00 worth of bonds.

They took that in payment for the work they did on the District, and they put in some—I don't know how many—[12] 45 miles of roads and 55 miles of canals, a warehouse site and a levee, and so forth, and the Reclamation Board of the State of California and the trustees of the Reclamation District approved the construction and the cost of construction and the issue of the warrant, and where Mr. Birch, after he got these bonds, purchased out the people known as the Hopkins who owned, I think, approximately a third interest with him and his part of the lands, and used the bonds to pay for that interest, \$786,000.00, and took the bonds at face value.

The law question involved is that whether a District so organized and bonds so issued, whether or not that District and those bonds lose their valid character, if such valid character it ever had, by virtue of Mr. Birch and his successor in interest, this Petitioner, having subsequently acquired all of the parcels of land in the District except one, and having subsequently again acquired all of the bonds. So, it just comes to—it is going to come down to just that plain and simple question of law, when all these facts that ought not to be controverted as before the Court, and the facts I have largely related by stating the question—those facts that I did relate

are contained—I don't know whether this detail is being helpful to your Honor or not, but I think it should help.

The Court: Yes, it is. [13]

Mr. Acret: Otherwise, it would be impossible to estimate the bearing of any of the evidence offered—those facts are contained in Judge Turner's findings. I think that case took three or four cases to present them, though there were many stipulations.

We are going to contend that with respect to the organization of the District, with respect to the issuance of the bonds, the holding of them as found by Judge Turner through a period of years up to and through 1939, the organization of this Petitioner and of the Birch Ranch & Oil Company, the owner of part of the lands in the District, that those facts are *res judicata* in this case. They are the identical—that is an adjudication of the identical principal issues in this case, as far as the basic facts are concerned.

The other case differed in that it concerned the right to make deductions on any accrual basis for 1937 and 1939, as I have stated, whereas this case involved the right to make a deduction for the amounts paid in cash for 1944.

The Court: Are these transactions that you speak of, of Mr. Birch, subsequent to Judge Turner's hearing, or was that involved at the time he found his findings of fact? In other words, what happened affecting the status quo of the parties subsequent to Judge Turner's matter?

Mr. Acret: What happened status quo is that,

as far as this Petitioner is concerned, times got better, and this [14] Petitioner had some money—the Birch Ranch & Oil Company, or rather, the Birch Ranch & Oil Company had some money, the owner of the land, and it was able to pay the taxes each year as they became due, and pay all the taxes to meet the past interest that had accumulated on the bonds.

The Court: Aside from the payment of taxes, what I am wondering about is whether or not the status of the parties, Mr. Birch's rights, as an individual, have they changed any?

Mr. Acret: Not that I can recall in any respect. The rights of this Petitioner changed, however, since the Commissioner filed the first report, and before it filed the second report, because in reliance on the first report, this Petitioner paid the deficiency assessment for 1941, and in reliance, on my advice, that its loss as shown for 1944, be entitled as a matter of law to be carried back to wipe out the 1943, so there is a good basis of an estoppel as well, on which I will have some authorities, and which I have in these points and authorities——

The Court: The matter of estoppel isn't in the pleadings, I guess.

Mr. Acret: No, your Honor, and I am going to have to ask for that. No matter how much we worked—in working on this case as it came up to-day, I found I should have plead both the estoppel and *res judicata*, and I think counsel will [15] not object. I have warned him and talked with him before with regard to this. I think he will not ob-



ject to my filing a second amendment to the petition, setting up the estoppel.

The Court: You don't have such amendment prepared?

Mr. Acret: I will have it over the week end, your Honor. I have been unable to prepare it. As your Honor knows, when we are in active practice, these matters—you get to finally preparing a case just before it is going to trial, and I have been doing that for the last five days, and I haven't been able to get out the amendment.

The Court: Does that conclude the statement of Petitioner's counsel, or do you have anything further?

Mr. Acret: No, it doesn't. There are a few more things I can state, which might be helpful.

Counsel and I, during the past week,—and counsel has been very generous and patient with me in an effort to arrive at a stipulation of facts. He undertook to prepare, and did prepare, a proposed stipulation which is taken from these findings of fact of Judge Turner, and from them he omits certain matters that he doesn't wish to concede, and which is perfectly satisfactory to me to have him omit. I can state that of the first 13 pages he has given to me——

The Court: Let the Court inquire; these matters admitted, you waive those?

Mr. Acret: No, the stipulation provides that either [16] of us may present testimony as to other matters, and we have certified copies of the record with regard to those. For instance, the Superior

Court of Yolo County provided by law, as soon as the Reclamation District was organized, there was a test case to determine the validity of the organization, and the Superior Court so determined.

The Court: The proof upon those matters admitted will be subject to your objections to Judge Turner's decision to hold them binding, or do you concede Respondent is right, Judge Turner's findings do not affect those matters you are going to offer in testimony?

Mr. Acret: Those matters are contained in Judge Turner's findings, the facts I just stated, and they are proper to be stipulated as facts in this case. The stipulation should include them, but we don't mind if they don't, because we can put it in evidence. Do I make myself clear on that? That is the situation.

The Court: I guess so.

Mr. Acret: As I say, I am willing to stipulate as to the first 13 pages, with just one minor exception, a slight inadvertence—slight inadvertent error in there.

Mr. Crouter: If your Honor please, I am very reluctant to make any comment at this time, but I do feel it is incumbent upon me to inform the Court that what Mr. Acret is now referring to is a final draft of a proposed stipulation of facts that he and I went over in considerable detail last week, and it was my understanding that it was agreeable and it was tentatively agreed to bind us. I had our office carefully make the draft, a copy of which he has, but to get to the point, we have not been able to

agree. It has not been agreed to up to this time. I am perfectly glad to have the Court umpire the situation of that sort, if you wish to, or we might do it informally, but we have been unable to agree at all that, and what Mr. Acret is now getting at is just an analysis of taking a part of the prior proceedings and seeing how much we should agree to as facts.

If Mr. Acret has any disposition over the noon recess to go into that matter again, I will be glad to talk to him. I don't think it is a proper matter that your Honor is interested in.

The Court: No, the Court wouldn't be in a position to assist in the stipulation of facts.

Mr. Crouter: It has been well understood, of course, if we cannot agree on those things, they will have to be proven.

The Court: The Court, in the interest of time, hopes they can be agreed to.

Mr. Acret: I think there is no question but what counsel is correct on that; if we can't stipulate, I think that your Honor could help us to do so informally, because it does seem if I can agree on the first three-quarters of what counsel offers, we at least ought to have that much. That is seven-eighths of the case, that first 13 pages, and the only others—the next 5 pages are just matters taken from Judge Turner's opinion, which relate solely to the other case, that is, what was done in the other years, the accrual entries for those years, and so forth, and they are not material to this case. It is the same way with the first two paragraphs—

The Court: It is your contention that the stipu-

lation of facts tendered by Respondent's counsel contain matters that shouldn't be in there?

Mr. Acret: That is right, they contain matters extraneous to the case and related to the other years.

The Court: I hope during the noon recess counsel will see if they can't reconcile the differences about what the contents of the stipulation of facts should be.

Mr. Acret: There are two more matters, and I will have finished my statement.

I believe I should call your Honor's attention to the fact that the only source of error that seems to arise here is by virtue of the interpretation of Mr. Birch's contracts with the Hopkinses, and they would be cleared up by this stipulation, and the other contention, it seems to make the error—it is overlooking the fact that the Reclamation Act [19] provides that a landlord may pay his assessment taxes to the County Treasurer with either bonds, or he may even pay the assessment itself with either bonds or with interest coupons, and the evidence will show that over a period of years Mr. and Mrs. Birch, when they first owned these bonds themselves, or a large part of them, and while they owned the land, they bought coupons from others, other owners of the bonds, and used these interest coupons and turned them into the County Treasurer.

Judge Turner—that is one error contained in his opinion, and it is the error the field officer makes in each occasion, and counsel states that is not a pay-



ment of interest, but Mr. Birch buys the coupons, and under the provisions of the statute, he pays the coupons into pay the taxes for the District. Though it is true he gives the money to an owner of the bonds to get the interest coupons, but the statute so provides, and I wanted to get that in your Honor's mind.

Now, this, over a period of years, was permitted at all times when Mr. and Mrs. Birch owned both the land and the bonds, and the transaction was questioned each time by the Commissioner, because Mr. Birch was in a position to make the deduction for the taxes, and yet, when the interest came back to him from the County Treasurer, it was exempt interest. That is the part that the Commissioner doesn't now [20] like. It is taking money out of one pocket and putting it in the other, and when your Honor analyzes the Act, you will find that between Mr. Birch's right pocket and his left pocket, even when he owned both the bonds and the land it was the law of California and the County Treasurer of Yolo County, and they were all matters beyond the landowner's control and the bondowner's control. It was just the operation of the laws of California, and there is nothing in the law that prohibits the landowner from owning the bonds, and we will show to your Honor that the Reclamation Act expressly permits it, and that is going to be the Petitioner's case.

The Court: Respondent's counsel?

OPENING STATEMENT OF BEHALF OF  
THE RESPONDENT

By Mr. Crouter:

If your Honor please, I would like to make some comment regarding the statutes of the proceeding at this time, and particularly the issues before the Court, and I will refer to some extent to the facts, but, as your Honor realizes, it is a situation where it goes back over the history of a corporation for about 20 years, and I hope I do not make it any more confusing.

To clarify the situation, as we begin, if the Court please, I am afraid the counsel inadvertently made an error in referring to the year 1943, because this proceeding, Birch Ranch & Oil Company, Docket No. 8720, when it was [21] originally filed, related to fiscal years ending September, 1941 and September 30, 1942.

Mr. Acet: I misspoke myself on that.

Mr. Crouter: And there were deficiencies for both of those years in income taxes, which aggregated \$19,749.11, and there were deficiencies determined in declared value excess profits taxes for both years, in the total sum of \$6,252.51.

Now, with respect to the prior proceedings, if your Honor please, and I don't say this to prejudice the record or either side's position, but in a nutshell, as I have read and reread Judge Turner's findings and opinion in the prior case, the question of accounting basis came up, and this same Petitioner corporation, there was accruing a liability payable

to the County on account of these Reclamation bonds, but the amounts were never paid at all, and Judge Turner held under the facts and evidence in that case that the Petitioner was, in fact, on the cash basis of accounting. Therefore, he did not have before him—and it was not necessary to decide this other question of legal liability.

That may help to explain the prior decision, and I would like to say that at page 21——

The Court: Judge Turner's decision merely held that because the payments were not made and the Petitioner was on a cash basis, the accrual of them didn't give the [22] right to deduct?

Mr. Crouter: That is correct, and they were not deductible.

The Court: Is that the only thing you are contending Judge Turner's opinion did hold?

Mr. Crouter: That is all he held precisely.

The Court: In his findings of fact, did he make any findings with reference to these other matters, as counsel for the Petitioner indicated? Do you agree with Petitioner?

Mr. Crouter: Yes, he did, in considerable detail, and most of those findings are included in our proposed stipulation of facts, which I hope we will be able to present after lunch.

Now, in the opinion of Judge Turner, he specifically held, as he stated at page 21 of the mimeographed opinion,—I will not read this paragraph, but he held, in effect, that in view of the conclusion reached and found—I will quote this, “We find it unnecessary to rule on the Petitioner's claim that

the bonds of Reclamation District No. 2035 were and are valid and subsisting obligations, constituting a lien or charge upon the property of the Petitioner, so as to entitle it to deduct so much of the amounts paid thereunder as is allocated to interest."

There is a little more along the same line, but [23] that shows what I want to bring to the Court's attention.

Now, to follow through on the procedural status of this case, there is no intervening proceeding, and there has been no litigation, that I know of, with respect to the fiscal year 1940. Just exactly why, I don't think makes any difference now.

For the years 1941 and 1942, fiscal years, a similar determination was made by the Commissioner, disallowing similar deductions claimed on account of the payment of interest or taxes on these reclamation bonds. That is the proceeding that counsel and your Honor referred to in this same case, Docket No. 8720, and in that case it came on for a hearing before Judge Kern, and——

The Court: When was the hearing before Judge Kern; how long ago?

Mr. Crouter: I have the exact date right in the brief here.

I have a little summary of prior proceedings in the whole case that might be helpful here. This is just a chronological summary of dates.

That was June 30, 1947, the case was presented to Judge Kern. Then on March 24, 1948, memorandum findings of opinion were entered, allowing rehearing, if requested. Now, the basis for that, as I



understand it, is this: You see, the case involves the net loss carry-back provisions of Section 122 [24] of the Code, and only with respect to the year 1942 however. You see, there is a question of a loss in 1944, and as counsel has stated, and I believe most of our evidence here and our attention will be directed to the taxable year 1944, but under the law that could only go back two years, and if established, it might go back to 1942. However, it was conceded in the prior case that it would not extend back to 1941, so, 1941, for all practical purposes, is out of this case, as I see it, although I may say that the decision, that is, the exact decision for the amount of deficiency due has not been entered yet as to 1941. The reason for that, as I understand it, is that only one decision would be entered as to the entire proceedings, and that apparently must await the Court's findings as to 1942.

Now, in 1942, and also in 1941, I believe there were accruals with respect to similar items of interest or taxes as deductions, but inasmuch as it had been held that Petitioner was on the cash basis, the Petitioner did not then reurge the same question which was litigated before. So there is no basis for allowing the deductions we are talking about for the year 1942, and I don't believe counsel will even propose to go into that.

I might also say as to the prior case decided by Judge Turner, it was appealed to the Circuit Court of Appeals for the Ninth Circuit and affirmed on appeal, and [25] certiorari was denied.

We will be glad to establish the official citation in the record at the proper point.

Now, to get down to the state of the case now, the issue before the Court, as I see it, is whether the Petitioner, during its fiscal year ended September 30, 1944, made payments of interest or taxes in the amount either of \$123,666.17, which is the exact amount claimed as taxes, on line 22 of the Petitioner's 1944 return, or whether the Petitioner may be entitled to a larger amount. I believe the Petitioners, in their amended petition, now claim that they are entitled to a deduction of two hundred twenty-one thousand, even or odd dollars, and the Petitioners claim that they did, in fact, make payments then, during the year 1944, to the extent of about two hundred twenty-one thousand, which, together with a great many other facts, of course, establish a net operating loss of the Petitioner for the fiscal year 1944, a large part of which would be carried back to 1942, and thus wipe out the taxable net income on which the deficiency for 1942 is based; so that we are litigating as to the taxable year 1942, but it is the facts as to 1944 which we must necessarily go into.

Now, as to Respondent's position, if the Court please, I do feel it incumbent to say just a few things here. Perhaps first I should clarify the record as to counsel's [26] position.

I might say that the exhibits received by Judge Kern in this proceedings, and that includes one copy of Revenue Agent's report——

The Court: Are those exhibits the ones that Petitioner's counsel referred to in his statement?

Mr. Crouter: Yes.

The Court: They were the ones presented to Judge Kern?

Mr. Crouter: That is correct.

The Court: And they are in the record now?

Mr. Crouter: They were received in the record just to show the fact there was such a controversy. They were not received by the Court, and certainly were not stipulated to or agreed to by counsel for Respondent as final facts in the case.

The Court: And they are not to be received now unless offered again for counsel's position?

Mr. Crouter: That would be my position. I do not agree particularly to the first Revenue Agent's report, because counsel for Petitioner already offered a portion, at least, of the first Revenue Agent's report. There was a later Revenue Agent's report for the same year, 1944, and your Honor will fully understand, I am sure, that while this question of cash basis or accrual basis and the question of [27] allowability or unallowability of these deductions was being litigated before the Tax Court, the Commissioner's position was a little bit uncertain, and it was more or less marking time with respect to later years, to see exactly what position the Respondent should or would take, and in that period of uncertainty, the year 1944 came along, just like other years do. Now, the Petitioner, in the supplement to the petition here—I would like to have Mr. Acret check me on this—as I see it, he has combined certain pages. He has three pages from the first Agent's report as an exhibit to his amended petition, and

then he has taken pages 1, 2 and 4 from the second Agent's report, and he has that as an exhibit to his petition.

Now, the second Agent's report, of course, is the one that the Respondent relies upon in this proceeding, along with the Respondent's own determination here that these deductions are not allowable. This is just one paragraph of the second Agent's report, page 2, which will show your Honor exactly what was determined, among other things that counsel for the Petitioner mentioned. Page 2, "Disallowance is made in the amount of \$21,610.87 claimed as tax deductions for the fiscal year ended September 30, 1944. This amount represents payments to the County Treasurer of Yolo County, California, for the purpose of paying interest on bonds of Reclamation District No. 2035. [28]

"This disallowance is based on the fact that there was no real or actual obligation outstanding against the taxpayer, since Reclamation District No. 2035 was comprised exclusively of the taxpayer's property, and since A. Otis Birch, and his wife, Estelle Birch, the sole stockholders of the Birch Ranch & Oil Company, hold substantially all the bonds of the Reclamation District."

Now, in the amended petition, the Petitioner pleads and relies upon the contrary position asserted in the tax returns. The Respondent in his answer took issue with that; and the answer to that part of the amended petition is just as clear as I believe it could possibly be made, making it very clear in the record that the parties are at issue over an allow-



ability of this two hundred twenty-one thousand dollars. So that the issue is squarely before the Court.

Now, upon that question of two reports and inconsistent positions, I am sure the Court is familiar with a great many cases. Unfortunately, sometimes those situations do arise. Respondent takes the position here that the last report, and certainly the position asserted formally in the pleadings before the Tax Court, represent the Respondent's final determination and his final position in submitting the questions involved to this Court and that the earlier report has been superseded and carries no weight whatever, either [29] as a final determination of any facts that may be involved, and certainly as to any legal question, and I believe this does run finally and chiefly to a legal question of allowability, based upon the California laws and our federal tax laws.

I am afraid that I cannot agree with counsel that all the facts are clear and undisputed. I believe that is evidenced by our difficulty in getting together, but we will still try to do that. Some facts are not agreed upon, if the Court please, particularly with respect to the organization of a Reclamation District by several persons dealing at arms' length, and for real business purposes. I will refer to things along that line a little later, but I do want to refer to two other issues before I get lost in the facts here.

With respect to two other matters that counsel mentioned, the question of *res judicata* and the question of estoppel; neither one of those has been plead in this proceeding up to this time, if the Court please. Now, it is true that counsel did mention to me as

long ago as a week or so ago that he might contend that prior proceeding is *res judicata*. My position at this time, if the Court please, and I have given a good deal of thought to this before this time and since counsel made his statement this morning, is that those are not issues in this case. I may say briefly that [30] particularly in view of Judge Turner's precise findings and holdings, I don't see how the plea of *res judicata* could have any merit. As to estoppel, Respondent's position is that—there is really no merit in that, either. The Courts have held many times the Commissioner is not estopped by a prior agent's report; there can be no estoppel, as I see it, as to the year 1941, because there is no possible carry-back to that year. There was no payment of taxes in that year. As I understand it, there was no payment of taxes in 1943 which could be carried back to 1941, so it is impossible for me to conceive what the Petitioner might rely upon for estoppel at this point.

The Court: Your position on that, however, would not be precluded in the right to plead estoppel?

Mr. Crouter: I was coming to that, if the Court please. We have had a great deal of difficulty with this case, as shown by our proceedings here. I believe that if those matters are seriously urged by the Petitioner, they should be reduced to writing. We should have them at the very commencement of the case, and at this point, although I am very reluctant to, I have to strongly object to any further inclusion of issues in the case. That is the reason it was

continued over and Judge Kern went into it. There was a question of whether the operating loss had been sufficiently pleaded in the case. As your Honor has probably discovered in [31] other cases, if it is an issue in the proceedings, then it must be determined in the proceedings. If a carry-back loss is not involved in the proceeding, the pleadings, then it can be litigated and determined later. So Judge Kern very fairly, and Respondent was in agreement with that, held the record open so that that question could be pleaded, so that the parties would know where we stand, go from there, and finally get to grips with this basic issue.

With respect to estoppel and res judicata, if the Court please, there are tremendous records connected with this case, in spite of what I have on my table, this is just a small portion of them, and I am not prepared at this time to go back into all of the prior cases and every element of estoppel. A number of agents worked on the case at different years, and some are out of the service now. I would have to make a round-up of witnesses, if counsel is really going into these issues. I don't think they are proper issues in the case, and I would like to have that question first determined by the Court, and my position would be that if counsel is serious on them and feels that should be included in the case, I am not disposed to deprive them of a chance to litigate anything they want to litigate in this proceeding, if it has any bearing, but I would have to ask that the hearing of the case be further continued so we can

have those matters in writing and know exactly what they contend. [32]

The Court: I think the suggestion that the pleadings be reduced to writing is a sound one. I think we frequently make a mistake by granting permission to amend without it being reduced to writing, but I do think Petitioner would have the right, should have the right to plead *res judicata* and estoppel, whether the Court might determine there was any merit in it or not, but suppose the counsel for Petitioner be given until we reconvene this afternoon to reduce those issues to writing, that is, *res judicata* and estoppel, and then counsel, of course, for Respondent would doubtless deny those. I don't know. There would be no affirmative pleadings.

Mr. Crouter: There would be a denial. As to the question of proof, *res judicata*, particularly, as I understand it, does involve everything that was previously submitted to the Court in the prior proceeding.

The Court: Wouldn't the record in the other case determine what was submitted to the Court in the prior proceeding?

Mr. Crouter: In a general way, if the Court please, but there are exhibits and testimony and things of that sort, and I do not have them. I will take oath and go on the stand, if your Honor wishes. I do not have everything involved in the prior case, and some things I want to examine. Your Honor is familiar with our system of closing cases year [33] by year and sending files back to Washington. I do not have all the prior documents and papers relat-



ing to the prior case, because I thought that 1937 and 1939 were certainly out of this case. I do have some of those, but I am afraid if broad allegations are made under *res judicata* and also under *estoppel*, I am afraid I would need further documents, and the Respondent would be seriously prejudiced by being in a position where he could not offer any evidence or having then to ask the Court to hold the record open and hear the rest of it at another calendar or in Washington. I would like to see it all brought together at one time and place and disposed of.

The Court: It is almost 12:30 now. Did you conclude your statement about the case? Let's leave that open right now. I am going to suggest that during the recess at the noon hour the Petitioner reduce to writing his pleadings on those issues, that is, *res judicata* and *estoppel*, and then we can take up at that time whether or not that would necessitate a postponement of the case.

Mr. Crouter: Does your Honor care to hear as to Respondent's position on the matters?

The Court: Yes, I was just indicating so that counsel will know.

Mr. Acet: With respect to that, I would like to state, your Honor, there is not any change in issues here in [34] the original petition. We alleged certain losses for 1944, and asked to be allowed to carry them back, but then when the Commissioner took the position we were on a cash basis, it made those losses different, and that is the basis of this amendment to the complaint.

Now, in the amendment——

The Court: We can discuss that when the pleadings are presented.

Mr. Acet: Yes, your Honor, but in the amendment to the complaint we allege and set forth Judge Turner's opinion, and, by the way, your Honor, it was admitted unconditionally in this proceeding, and I contend that this proceeding is merely a further hearing of Judge Kern's proceeding, and that the document is in evidence, the findings of fact, what they are, and there are no new facts to be alleged, and all we need to do—and I proposed it to counsel—at the end of the second paragraph is to insert the legal conclusions. That is all we need to do.

The Court: In the meantime, counsel will do that and then after we reconvene we will take up the question of the effect of the pleadings.

Mr. Acet: I was proposing to just ask leave to insert the words, "that such decision is res judicata of such."

The Court: Are you ready now to amend your pleadings? [35]

Mr. Acet: Yes, your Honor, just by interlineation.

The Court: You can do it right now and submit it to counsel.

Mr. Acet: It is to interline at line, the third line on page 2, at the end of the paragraph, the words, "that such decision is res judicata of such issues here." That is all that is necessary. Then to

add a paragraph, and I will draw that up and ask to insert that by interlineation, "That subsequent to such filing of such second report—" I am not following the wording closely here now—"the Petitioner, in reliance thereon, paid said deficiency assessment for 1941, and the Commissioner should be estopped from asserting facts against this Petitioner different from those therein contained."

The Court: Counsel can have that prepared by the time we reconvene at 2:00 o'clock, and counsel for Respondent can now conclude his statement on the merits.

We understand the amended pleadings will be taken up at 2:00 o'clock and I would like for Petitioner's counsel to have that amendment ready in writing.

Mr. Acret: Yes, your Honor.

Mr. Crouter: With respect to the merits of the question of deduction of interest or taxes for the year 1944, if the Court please, the Respondent's position is that no deduction is allowed, or are allowable in accordance with [36] the determination and this last report, for various reasons. There are several, and there is a little overlapping, but I might just in a general way mention them so the Court will know Respondent's position as we go along with the evidence.

The basic one is that Respondent contends that there was no Reclamation District ever organized, and that there were no bonds ever issued and outstanding during any of the taxable years involved here upon which such deductions could properly be

recognized. This, of course, goes back to the formation of the District and the number of people in it. The basic reason there is, as the evidence will show, the Petitioner corporation acquired ranch property that was previously owned by the Petitioner and certain other persons, mostly very close relatives. The evidence will show that there was certain reclamation work done, about two million dollars, or a little over that, but the money was all advanced and the work was done by Mr. Birch or Mr. Birch's corporations; that the others may have contributed something, but a very small portion of it. I believe that from the beginning the evidence will show that there was some disagreement between some contiguous landowners and certain ones dropped right from the start and were not in it.

Just to stick to the legal questions, Respondent's contention is that there was no original issuance of bonds; that is, back in about 1925, I think. [37]

Now, it is a long story and we will all have to have some patience. There were bonds that they claim were issued which are affected here, and they were 10-year bonds. They were all to be paid off in 10 years. I think the face amount was \$227,000.00 for each one over a 10-year period, and they contemplated apparently that \$2,227,000.00 would be paid back, and all of the liens and everything wiped out and erased by that 10 year period, by the expiration of it, in other words, about 1935.

It is my understanding that the Petitioner contends that there was a reissuance or a refunding of some kind of bonds about 1935, and that is one of



the points particularly on which the facts will have to be secured, and the Respondent has never been shown, much less convinced, that there was, in fact, a real reissuance of bonds at that point, about 1935, which is, of course, prior to all the taxable years on which the Petitioner could pay any amounts as taxes or interest, which would be recognized as such.

So Respondent asks for proof on the issuance of those bonds and the original formation of the Reclamation District, insofar as it involves the question of a taxpayer and his own solely owned corporation dealing with and among themselves in the organization of a district like that, and the setting up and claiming of tax deductions.

The evidence will show the Court and the facts, I think [38] will be clear on this, that at first there were accruals of liability, and the corporation would take a deduction. The corporation, of course, owned the land, and there were assessments on the land, and then the bonds were issued and outstanding, and Mr. Birch and some other persons held some of those bonds.

Moneys would be paid to the County Treasurer at 6 per cent on the \$2,000,000.00; that makes \$120,000.00 each year, and the corporation for some years would accrue the liability and taking a deduction of \$120,000.00 each year. That, of course, was claimed as a federal tax deduction.

Now, the way this operated, if the Court please, and I think the facts will be clear on this part of it, was that usually contemporaneously with a payment to the County Treasurer, who was, under the statute,

a party to such a Reclamation District, payments would go into the County Treasury from the corporation, and payments would go from the Treasurer back to the individual, as interest. Now, that was interest on the bonds which were held by the individuals, held and owned by them, and that under the procedure set up, it was received as tax exempt interest, so that the Petitioner—not the Petitioner, but Mr. Otis Birch and his wife individually did not ever report taxes on the interest received from the County and through this system. [39]

Now, that apparently was set up and operated a great deal. If we have to go into the whole history of this thing, I believe the evidence will show that more than \$2,000,000.00 went into the County Treasurer's office as a payment of interest; more than \$2,000,000.00 came out of the Treasurer's office as tax exempt interest. I believe that the record will show that this Petitioner was organized and operated ranch properties, including several sections of good farming land, and so forth, and that over a period of 20 years it never paid one dollar of federal tax to the Federal Government, under this system as it operated.

The Court: The only parties before the Court now is the corporation, as I understand it?

Mr. Crouter: That is correct. If the Court please, the Respondent contends that this whole Reclamation District, and that this system of making payments allegedly of taxes or interest to the Reclamation District and the taking money out, that was

just a fiction, it having no real substance that should be controlling for federal tax purposes.

Now, I don't believe it is altogether controlling, whether the Court finds ultimately there was or was not a valid Reclamation District to begin with. The situation 'way back in 1918 and 1920, when it started off, was vastly different, and the interests were vastly different from what they were a few years later and long before 1935. Those [40] first bonds apparently expired by their terms, and the State laws will have a bearing on this. We will show to the Court during the proceedings, or on brief, that bonds are supposed to be paid off, and when they are not paid off and in default, it is the duty of the State officials to foreclose on the property and take it. That never happened in this case. As a matter of fact, the evidence will show that during the depression years a great many years went by and there was no payment to the County Treasurer and there was no payment from the County Treasurer, because money apparently was not available, and the whole thing was more or less abandoned.

Now the Respondent contends that the corporate entity here should be ignored. The evidence will clearly show, as counsel stated in Petitioner's opening statement, that the petitioning corporation was wholly owned by Mr. and Mrs. Birch, if not directly through one of their holding corporations. I believe it was through another corporation during most, if not all, of that time, but regardless of whether there is only one corporation or two corporations, that is essentially Mr. and Mrs. Birch.

Respondent relies upon certain decided cases, but I will not mention those. There is a prior case of the Board of Tax Appeals involving the question of income or loss as between certain corporations in a Bond District, and that is the Rindge Land & Navigation Company case, 2 B.T.A., 1179, and [41] various other authorities that the Respondent will rely upon.

Respondent, among other things, relies upon another contention, and that is that under California law, under General Real Estate Law, and under the facts which will be shown here, there was a merger of all interests and titles and holdings of Mr. Birch in himself or for himself and this corporation, so that any liens on the property and obligations on the property were merged with the ownership itself; so that Mr. Birch was really, in fact, going through the form of paying from one pocket to the other; that deductions, of course, are a matter of statute, and that is, this is not a case of any real tax or any real interest that should be recognized for tax purposes.

Respondent further contends this was not a part of any real business, of a business corporation, but it was a peculiar arrangement which certainly had its tax advantages, if it would stand up, but it should not be recognized and certainly was not contemplated either under the original Reclamation Act of the State or the Revenue Act.

Now, as to the revenue acts, the Court is familiar, of course, with the provisions of Section 23 B. of the Internal Revenue Code, and the Court will recall



—with the Court's permission, I would like to read it:

“Interest—All interest paid or accrued within the taxable year on indebtedness, except on this indebtedness incurred or continued to purchase or carry obligations (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from the taxes imposed by this chapter.”

Now, you see, that says interest generally is deductible on this indebtedness. Respondent will contend that under this statute and under the decisions based upon this statute, we have here in this case the very simple situation of a system and mechanics set up and followed to create this tax exempt interest, so that any expense or any disbursements made in connection with that is not to be recognized as an interest payment for the additional reason that it is merely a part of the securing of tax exempt interests.

I should also like to state, if the Court please, that Respondent directly contends that the continuation of this system of havings bonds outstanding, of never retiring the principal but leaving it outstanding—and I may say that, as I understand it, Petitioner will attempt to show that in about 1935 in connection with their refunding, they not only extended it for 10 years, but extended it clear through 1984, so, you see, this is a basic question we might as well have determined, so we don't have to litigate every year before 1984.

The Respondent contends this is just a tax [43] avoidance arrangement, and I say that respectfully, with no discourtesy to Mr. Birch. He has attempted to do what he thought he could do legally, but it has never been done either in this petition or any other.

The Court: Have you been able to find anything on the question of merger?

Mr. Crouter: There are State decisions, and I will be glad to cover that in the brief.

The final point, the carry-back statute also has certain exceptions and limitations, and there, of course, any loss incurred must be incurred in connection with regular business operations.

Respondent will contend in brief, I believe, that whatever may have happened in 1944, it was not a regular part of ranch or oil operations, and even under the carryback statutes, Section 122 of the Code, the facts will not establish a loss which could be carried back to wipe out any deficiency which the Commissioner has determined for the year 1942.

Thank you very much.

Mr. Acret: Just one position that the Petitioner takes, and for me to convey that to your Honor may be helpful at this time, and I overlooked stating in and will answer counsel.

He brings the crux of the situation down to [44] whether or not a person has a right to own a lot of land and bonds on it, and deduct the interest and receive back the interest as exempt.

As I say, the Commissioner permitted Mr. and Mrs. Birch to do that for years, and under the laws of the State of California, it expressly provided the

exempt interest for the purpose of encouraging men like Mr. Birch to do this very thing. In other words, he went in and spent \$2,000,000.00 under the provisions of the Reclamation Act and the laws of the State of California on land no good, developing swamp and marginal lands on the basis he could do this or otherwise he wouldn't do it. He took lands absolutely worthless and spent \$2,000,000.00 on them, because you can put bonds on them, with the ultimate idea he possibly could, if he wanted to, put bonds on them and have it as exempt interest.

I have cases in my memorandum that say the purpose of the law is even to "coerce," using the expression, in the development of these marginal lands. When the State of California has tried to do this, the government has tried to take away the benefits.

Insofar as not paying the first bond issue, lots of people couldn't pay the bonds in the depression period. When I was in Washington—I don't know the situation here—but lots of property owners couldn't pay, but the government extended our chances and was lenient with us during the [45] depression. This company paid as soon as it could, and paid all the interest up to date, but couldn't do it before.

Does your Honor want me to hand one of these to the Clerk, these Points and Authorities, which shows opposition with respect to the provisions of the Reclamation Statutes. Your Honor, this is going to be decided by you, I am sure, solely on the provisions of the Reclamation Statute of California.

The Court: I think that would probably come a little later, wouldn't it? Is that the extent of the legal authorities sustaining your position?

Mr. Acret: Rather a statement of our position and the authorities supporting it.

The Court: We are going to take a recess until 2:00 o'clock, and at that time the Court would like counsel for Petitioner to have formally prepared and presented his plea upon those two issues, and counsel for Respondent will then be heard and Petitioner, also, upon that issue.

We will take a recess until 2:00 o'clock.

(Whereupon, at 12:45 p.m., a recess was taken until 2:00 p.m. of the same day.) [46]

### Afternoon Session

The Court: Is counsel ready to proceed in the case?

Mr. Crouter: I believe so, if the Court please.

Mr. Acret: Yes, your Honor. May I proceed?

The Court: Yes.

Mr. Acret: At this time, your Honor, I present to the Court the proposed amendment.

The Court: An amendment to Petitioner's amendment?

Mr. Acret: A supplement and amendment to the petition, which consists of the insertion on Page 2 at the end of line three, the following words, "That such findings of fact are res judicata of such issues herein," and the insertion, at Page 5, after paragraph eight, to wit, the last paragraph thereof, the



following: "That subsequent to the filing of the report referred to in paragraph three hereof, and in reliance upon the position taken by the Commissioner in such report in the respects of foresaid, this Petitioner did, on July 7, 1947, pay to the Commissioner in full the deficiency assessment involved herein for the year 1941, together with interest thereon, to wit, the sum of \$12,398.85; that by reason of the facts alleged herein, Respondent ought to be and is estopped from changing his position herein with respect to this Petitioner having suffered such loss in 1944 and with respect to this Petitioner's right to make such deductions of \$120,000.00 for such year for taxes paid by it to enable such [47] reclamation district to meet interest for such amount in such year upon such bonds."

That is the amendment, your Honor, and I have handed to the clerk a page stating those insertions and where they would go, and she proposes to insert them in the file in the appropriate place.

The Court: The amendment will be received and filed as a part of Petitioner's pleadings in the case.

Does Respondent desire to make any reply to the amended pleadings?

Mr. Crouter: I would like to make a written denial, if the Court please. I would like to have permission to file a written denial of the allegations made, but I am ready to proceed.

The Court: That permission is granted.

Mr. Crouter: I would like to observe and just call to the Court's attention that as to the estoppel question in the year 1941, that year, of course, is directly

at issue in this proceeding. It is true there have been prior proceedings on it, but it is still the same year that is involved in the case before the Court, and if the Petitioner had any position that it wished to save or assert in this proceeding, it is still open, so that does not go beyond the very years before the Court here.

Mr. Acret: We made some statements when Judge Kern [48] conducted the hearing, stating that we abandoned the allegations and claim in our petition with reference to 1941. I forget just how it was worded, but he just stated it would be noted in the record, or something to that effect. It is understood we not only abandon the position taken with reference to 1941, but we have since paid the amount involved, with interest. At this time, your Honor, I presume we present jointly the stipulation of facts for filing herein, which, I believe, your Honor has read.

The Court: The stipulation of facts will be received and filed as part of the record in the case.

Mr. Acret: At this time we offer in evidence receipt of the collector of internal revenue, dated July 7, 1947, for said sum of \$12,398.85 for the payment of said deficiency assessment for the year ending September 30, 1941.

Mr. Crouter: No objection.

The Court: It will be admitted as Petitioner's Exhibit No. 1.

Mr. Acret: May it be number 4, your Honor; there are three already numbered.

The Court: They haven't been formally presented, have they?

Mr. Acret: I will, if your Honor please.

The Court: Present those first.

Mr. Crouter: There are numbered exhibits in [49] connection with the prior hearing in the same case.

Mr. Acret: I will re-present them, then.

The Court: I think you had better re-present them. There are no exhibits contained in the stipulation, as I recall.

Mr. Acret: No, your Honor.

Mr. Crouter: That is correct.

Mr. Acret: At this time, in support of the pleadings, relative to *res judicata* and *estoppel*, and for all purposes, the Petitioner offers, reoffers for re-admission Exhibit No. 1, which was heretofore admitted as such Exhibit No. 1 in the prior proceedings in this matter.

The Court: What is the document? Identify it by some name that will indicate what it is.

Mr. Acret: Exhibit No. 1, the Reporter's transcript shows it to be a 30-day letter of the internal revenue agent in charge, dated January 22nd, it seems to be, with three pages attached. The Exhibits ought to be in the file, should they not, bound in?

The Court: That was Exhibit 1 in the hearing before Judge Turner or before Judge Kern or both?

Mr. Acret: Before Judge Kern.

The Court: Does the clerk have those Exhibits in the record here, filed?

The Clerk: They are not in the file. [50]

Mr. Acret: Your Honor, the Exhibits must be separate from the file.

The Clerk: They don't usually clip them in the file.

Mr. Acret: As I understand it, and from this record, it appears there is an inadvertent misstatement on my part as to the year. The Exhibit 1 should be the first report of the internal revenue agent in this matter.

The Court: What date is that?

Mr. Acret: I don't have the date of it. The first page is gone.

The Court: Is the document there? It might have been introduced before and not now contained in the record of the file. The clerk wants to mark them as being introduced.

Mr. Acret: They should be with the file. If they are not here, they can't be reintroduced. Would counsel supply me with a copy of the first report?

Mr. Crouter: I don't believe I have a copy of that Exhibit that went in evidence.

Mr. Acret: Well, counsel has a copy of the first report that contains the allowance of the deductions. It fixes the loss in the amount of \$221,000.00.

Mr. Crouter: To answer the Court's question a while back, the Petitioner has attached to his first amendment to the petition what appears to be the transmittal letter with that first report, and that is dated January 3, 1947. Now, [51] if your Honor please, I would like to say, as to this matter, that I would have to object to that first revenue agent's report going into evidence, for the usual grounds that



the Respondent objects in such cases, and that is that it has been superseded, that it is not evidence of any fact or alleged fact or statement contained therein, and that it is not binding upon the Commission, particularly when the Commissioner and a different agent at a later date have made a different and contrary finding and determination. I would say, however, I have no disposition to keep that out of this record, insofar as it was received before. I would like to explain to the Court that at the proceedings before Judge Kern, on June 30, 1947, as shown at page 41 of the transcript, at that time the Court ruled upon this very matter and received that report on a conditional basis as to the 1944 loss, and the Court stated: "I understand the revenue agent's letter to which counsel refers will not be submitted as proof to any of the facts set out therein or the existence of the losses referred to, but merely to prove that at the present time there has been an official recognition on the part of Respondent there may be a net loss allowed in 1940."

"Mr. Acret: That is it exactly. Further than that, counsel doesn't need to worry. We are conceding the matter may be left open. We are conceding it isn't any decision on the merits." [53]

So, it seems to me that shows the report is in the record for whatever it is worth.

Mr. Acret: This is offered. We are setting this up as an estoppel, because since Judge Kern's ruling, we have done something; paid \$12,000.00.

The Court: The Court will admit it for all purposes, and the effect will be given later.

Mr. Acret: Very well. I haven't the transmittal page that goes with it, but I have here the two inside pages that contain the matter that shows the position taken by the Commissioner in his letter of the date stated by counsel. That is a preliminary statement that says, "For the history of the taxpayer, see a prior agent's report in U. S. Tax Court findings of fact and opinion in No. 109,993," and then in that they show how they changed the loss we took for 1944 from eighty-four thousand to a hundred and eighty-six thousand dollars, by reason of allowing us this deduction of the money paid as taxes.

The Court: What counsel just stated, is that contained in Exhibit or is that something additional?

Mr. Acret: This is two pages of the Exhibit, for your Honor's present information.

The Court: The Court wants to be sure that the Exhibit speaks for itself, and that it is received and marked by the clerk so we may know it is a part of the record in this [53] case.

Mr. Crouter: May I inquire, are those pages two and three from the first agent's report or the second?

Mr. Acret: The first agent's report.

Mr. Crouter: I wouldn't object to that. If the other complete report is in the record, I think that would be enough. I have no objection to counsel showing that to the Court for his information as we proceed here, but I don't see this needs to be offered or received in the record, and I object to anything

contained in it, on the same grounds I objected to the other one.

The Court: The Exhibit hasn't been located yet.

Mr. Acret: Your Honor, it was put in.

The Court: I mean, it is not here. The Court wants to know if the Exhibit is here now.

Mr. Acret: Apparently not, but I have a photostatic copy of two pages.

The Court: Why can't we submit the photostatic copy if we know it to be correct, because it may be lost or misplaced. When the Court goes to determine this case, he wants to be sure the evidence offered is available.

Mr. Crouter: It seems to me counsel should furnish a complete report.

The Court: I think the whole document should be offered. [54]

Mr. Acret: I put it in evidence, your Honor, and put it out of my power to do anything further with it, except insofar as I may happen to have a photostatic copy.

The Court: Does counsel agree that is a correct photostatic copy?

Mr. Crouter: It appears to be, the first four pages, at least. I am not able to tell whether that is all of it, but that is the first three pages, with the transmittal letter.

Mr. Acret: We offer the four pages in question, your Honor, photostatic copies.

Mr. Crouter: To which Respondent would like to have the objection on record, if the Court please, that this is a first revenue agent's report, which has been entirely superseded by a later agent's report,

a copy of which has been made a part of the Petitioner's amended and supplemental petition, and on the ground that this first agent's report is inconsistent with the Commissioner's determination in this case; it is inconsistent with the Respondent's present position in this case and any matters or conclusions or alleged admissions contained therein are not binding upon the Respondent.

Mr. Acret: It is understood it is offered as the basis of our having paid the \$12,000.00.

The Court: The effect to be given the testimony will be determined. It may not be given any effect, but it will be admitted, subject to the objection of Respondent's counsel, [55] and he has his exceptions on the grounds stated. Now, that photostatic copy is admitted in lieu of the original, unless the original can be found.

Mr. Acret: Very well, your Honor.

The Court: The clerk has that now?

The Clerk: I am going to mark it Exhibit 1.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 1.)

Mr. Acret: At this time we offer by reference the findings of fact of this Court in Docket No. 109,993, which were admitted as Exhibit No. 2, generally admitted, in this matter, in the former proceeding.

The Court: What is that document?

Mr. Acret: That is the findings of fact of Judge Turner in 109,993.

Mr. Crouter: If your Honor please, Respondent



very respectfully objects to the receipt of this document as a summary or complete statement of the facts in the case, for the following reasons: The matters contained in the findings there, of course, do have some bearing upon the matters which are involved here, but I don't fully understand counsel's position in that regard, because the stipulation of facts which we have entered into contains verbatim paragraph after paragraph, at least nine-tenths, I believe, of the findings of Judge Turner in the prior memorandum opinion, and that is [56] exactly what most of our findings are based upon. In a general way, the things that are in the findings that are not in the agreed statement of facts, in my opinion, and with all due respect and deference to Judge Turner, are things in the nature of conclusions as to the validity of certain proceedings or invalidity of them, and things of that character, which appeared to me to be conclusions.

Now, counsel has offered as evidence things of that character which he has deleted from the stipulation of facts. I did not know he was going to turn around and offer that as such, and I object. I do not believe the matters contained in these constitute facts and should not be received by the Court in this proceeding. I am inclined to think Judge Turner would rule that way.

Mr. Acret: I think this is admissible for two reasons; in the first place, it is in evidence generally as Exhibit 2. I offered it generally. I stated, "At this time we offer the findings of fact to the Tax Court in Docket 109,993——"

The Court: What are you reading from?

Mr. Acret: Page 43 of the Reporter's transcript of the proceedings in this matter, which took place June 30, 1947, before Judge Kern. Counsel made objection. After two or three pages of argument, the Court stated, "Well, I think that will have to go in one way or another for one purpose or another." The [57] Court said, "I will overrule the objection and it will be admitted in evidence."

So, it is in evidence as No. 2.

Further than that, No. 1, which has just gone in, being the report of the Commission, states that "For the history of the taxpayer, see prior agent's report in United States Tax Court findings and opinion in 109,993," and that is the findings of opinion, and it is necessary to have that to connect this up.

Also, the third reason is that it is admissible now, and I am offering it again for the reason that there is since intervened a new issue, and that is that those findings of fact are *res judicata*, and we offer them in support of that issue.

Mr. Crouter: If your Honor please, I do not wish to be contentious about this matter, but I again have to refer to the proceedings before Judge Kern on June 30, 1947, a transcript of which, I take it, would be with the Court's file, and the same document was offered at the hearing before Judge Kern, and the Court inquired whether there was objection and I made objection somewhat along the same lines that I have objected here, and perhaps some additional grounds, and then the Court stated, at page 44: "I question how important any of those facts

contained in the memorandum and opinion and findings are in this case. Ultimately the question I have is a procedural question.” [58]

If I may just interpolate, the Judge was still there concerned as to whether the net loss carryback was an issue in the case. Now, omitting some of the colloquy, on page 45, I made the further statement:

“Mr. Crouter: I have no objection to that going in merely for the Court’s information, and for consideration in making its ruling an order with respect to the net loss carryback question. I do not concede all the matters stated there are facts, and I do not wish to have the Commissioner prejudiced in any future proceedings of that kind in Court or out with respect to anything I do now regarding this statement.

“The Court: Well, I think that will have to go in in one way or another, for one purpose or another, that finding of Judge Turner.

“Mr. Crouter: Yes.

“Mr. Acret: Whatever the legal effect of that is is another matter. That results just as a matter of law.

“The Court: I will overrule the objection and it will be admitted in evidence.”

Then it was received in evidence, as shown at page 45. I submit it was not received for all purposes before, and I think Judge Kern recognized—— [59]

The Court: Well, there has got to be a lot of unscrambling done here in reference to what has gone before. In order to do that intelligently, and without

making any commitment, I think it should be admitted. I will overrule the objection. That will be admitted as Petitioner's Exhibit No. 2. Does the Clerk have the Exhibit there?

The Clerk: No.

Mr. Acret: That can be No. 2 by reference, and the record will show that. That was in a memorandum opinion, was it?

Mr. Crouter: That is right.

The Court: What is the number of the memorandum opinion?

Mr. Acret: 109,993.

The Court: Have the Clerk indicate there the document number and the date of the memorandum opinion.

The Clerk: That was a finding of fact of Judge Turner?

Mr. Acret: 109,993.

The Court: And entered when? Does counsel have that date?

Mr. Crouter: My file indicates that was entered April 20, 1944. If the Court please, may Respondent have an exception on the rulings on Exhibits 1 and 2, if that is necessary? [60]

The Court: Yes. That is Exhibit 2.

(The document above referred to was received by reference as Petitioner's Exhibit No. 2.)

The Court: Now, what is Exhibit 3?

Mr. Acret: Your Honor, we reoffer in evidence Exhibit 3 in the formal proceedings herein, which is Petitioner's income tax return for the year ending



1944. Does counsel want to put in, furnish the original of that?

Mr. Crouter: Yes, Respondent would be glad at this time to offer the original.

Mr. Acret: I was just going to take it as our Exhibit 3.

Mr. Crouter: It is necessary for Respondent to keep an exhibit number. We can make it a joint exhibit.

The Court: Joint Exhibit 3-A.

Mr. Crouter: And that will be the original of the income and declared value, excess profits tax return, Form 1120, of Birch Ranch & Oil Company, the Petitioner herein, which was filed in the Sixth California Collection District.

Mr. Acret: For the year ending September 30, 1944.

The Court: Fiscal year ending September 30, 1944. That will be admitted as Joint Exhibit 3-A, and leave will be granted to substitute photostatic copies.

(The document above referred to was received in evidence and marked Joint Exhibit 3-A.) [61]

Mr. Acret: May it be stipulated here, counsel, before I forget it, in case it isn't in our stipulation, that counsel's system of accounting is at all times material on the basis of a fiscal year ending September 30th.

Mr. Crouter: That is correct, and I so stipulate it.

The Court: On a cash accrual basis?

Mr. Acret: We are adopting, on account of the reports, a cash basis. We are consenting to it in this instance. It makes no difference whether it is accrual or cash, because the only item involved, we paid. Another thing, so there will be no misunderstanding, counsel made it clear to your Honor, I think, but if we are not entitled to the hundred and twenty thousand dollar deduction, we will owe the deficiency for 1942. In other words, it takes at least about \$14,000.00 to be able to carry back out of a hundred and twenty thousand dollar deduction, or we are not entitled to anything.

Mr. Crouter: I believe that is a fine thing to stipulate. There are no other issues or matters relating to the fiscal year 1942, which are left open or still pending or as to which the parties are at issue. In other words, as to the year 1942, it is closed, except the one question of a carryback loss from the fiscal year 1944 to the fiscal year 1942.

The Court: Does Petitioner's counsel agree to that stipulation? [62]

Mr. Acret: Yes, and I bring that up because I think it would reduce your Honor's labor, if you could make some kind of a note.

The Court: The record will show that.

Mr. Acret: At this time we offer Exhibit 4, which is the receipt.

The Court: That is what you started to offer a while ago?

Mr. Acret: I have shown it to counsel.

Mr. Crouter: No objection.

The Court: State again what that is.

Mr. Acret: A receipt of the Collector of Internal Revenue, dated July 7, 1947, for payment of \$12,-398.85. It says, "For fiscal year 9-30-41."

The Court: And that is a payment made by the Petitioner in this case?

Mr. Acret: The receipt runs to Birch Ranch & Oil Company, the Petitioner herein.

The Court: It will be received as Petitioner's Exhibit No. 4.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 4.)

Mr. Acret: Further than that, your Honor, to clarify the record, that relates to the deficiency assessment involved herein for the year 1941, which this Petitioner—concerning [63] which this Petitioner heretofore abandoned.

If your Honor please, I will take some of the matters which counsel didn't or for which some reason we didn't include in the stipulation, and I am showing counsel now three exhibits.

Mr. Crouter: Respondent has no objection to these documents going in evidence in this proceeding, if the Court please. I wish to state, however, that we do not concede everything contained in the documents.

The Court: You refer to the three documents that Petitioner's counsel is now about to offer in evidence?

Mr. Crouter: That is correct, if the Court please. We do not agree as to any conclusions shown on the

documents or conclusions Petitioner may draw from them, but they are documents which have some bearing upon the issues.

The Court: They will be offered now as Petitioner's Exhibits.

Mr. Acet: I will state what they are.

The Court: The first will be Exhibit No. 5, and what is that?

Mr. Acet: At this time the Petitioner offers a document to be marked Exhibit No. 5 herein, which was heretofore Exhibit No. 15 in the proceedings No. 109,993, said document consisting of the judgment role or an action in the Superior Court of the State of California, in and for the County of [64] Yolo, in the matter of the legality of the existence of Reclamation District No. 2035, and the same consisting of the complaint in such proceeding, the affidavit of publication, certain exhibits, the findings of fact, and the judgment therein, and other documents.

The Court: Judgment of what, some court?

Mr. Acet: The Superior Court of Yolo County.

The Court: California?

Mr. Acet: California, and the complaint is entitled, "To Determine the Legality of the Existence of Reclamation District No. 2035."

The Court: All of those papers are contained together, are they?

Mr. Acet: Fastened together. I imagine there are 20 or 30 pages, and the judgment purports to find the proceedings——

The Court: What is the date of the judgment?

Mr. Acet: The judgment is dated June 29, 1920,



the time of the formation, shortly after the formation.

The Court: It will be received in evidence as Petitioner's Exhibit No. 5.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 5.)

Mr. Acret: At this time we offer an instrument proposed to be marked as Petitioner's Exhibit No. 6, the same being [65] and purporting to be a certified copy of the judgment role in an action in the Superior Court of the State of California, in and for the County of Yolo, and entitled, "Reclamation District No. 2035, Plaintiff, versus The Lands of Reclamation District No. 2035 and All Persons Owning the Same or Interested Therein, Defendants," and the judgment therein, purporting to pass upon the legality of the first two million dollar issue of bonds, Nos. 1 to 2,265, and dated, and if your Honor will mark this, from January 1, 1935, when the first group of 227 came due, to January 1, 1944. That is when the last one became due in that first issue.

The Court: That will be admitted as Petitioner's Exhibit No. 6.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 6.)

Mr. Acret: I am emphasizing that because it is somewhat at variance of counsel's understanding of the facts, as indicated by part of the opening state-

ment. The bonds were 20-year bonds, instead of 10-year bonds.

Mr. Crouter: If your Honor please, Respondent's position on that is exactly the same as to Exhibit No. 5.

The Court: Yes, I understand Respondent has an exception.

Mr. Acet: I emphasize that for your Honor's information at this time. That is Exhibit No. 6. [66]

We offer in evidence at this time a certified—and by the way, that last Exhibit was also an Exhibit in the former case.

The Clerk: This is a certified copy?

Mr. Acet: This is a certified copy. We offer in evidence at this time an instrument proposed to be marked as Petitioner's Exhibit No. 7, the same purporting to be a certified copy of the judgment role in an action in the Superior Court of said County and State, in the matter of the legality and validity of refunding bonds of Reclamation District No. 2035, authorized at an election held in said District on December 4, 1934, the complaint entitled, "Action to Establish Validity of Refunding Bonds Aggregating the Principal Sum of Two Thousand Dollars."

The Court: Now, that is admitted that those bonds are the bonds involved here?

Mr. Crouter: No, that is not admitted.

The Court: I don't know what the number of the district is. Is the number of the district contained in that the same as number of district the Petitioner owns and has?

Mr. Acet: 2035.

Mr. Crouter: The same Reclamation District. There is a question of issuance and reissuance of bonds, if the Court please, and I don't know whether that brings it through the taxable year or not. [67]

Mr. Acret: We will connect it up.

The Court: I wanted to be sure these matters were related to the matters before the Court.

Mr. Crouter: Respondent's position is the same as to Exhibit No. 5. Respondent admits there are some relevant matters shown there, but does not wish to be bound by any of it.

Mr. Acret: I take it, your Honor, it is helpful for me to summarize, by way of information, as we go along, the contents of these, so your Honor will follow the chronological progress. We will connect this up. The complaint alleges——

The Court: You are referring to Exhibit No.——

Mr. Acret: Proposed No. 7. The complaint alleges the issuance of the election for refunding issuance of refunding bonds, the issuance of the outstanding bonds of two million dollars, heretofore referred to in the former Exhibit, and lists them, and that is a copy of the Notice of Election, the certificate of the results of the election, and the listing and issuance of the refunding bonds, coming due, commencing January 1, 1945, and up to January 1, 1948, in the total amount of \$2,000,000.00. It contains the allegations of the various proceedings, and it contains the resolution of the board of trustees, with relation to said former issue and of said new issue, and a complete list of the bonds and a receipt of the county treasurer for such new issue of the bonds, the

same being [68] No. R-1, the "R" I presume standing for refunding; 2-R, two thousand, totaling \$2,000,000.00, and the judgment, the document contains affidavit of publication, an order——

The Court: What is the date of the judgment?

Mr. Acret: ——notice of publication, summons, and the date of judgment is—the judgment recites apparently the same as the complaint, findings, the issuance of the bonds, and is dated June 25, 1935.

The Court: That will be received as Petitioner's Exhibit No. 7.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 7.)

Mr. Acret: And I have a copy of bond number 2,000, a photostatic copy. I don't know whether counsel will take my word for this or not. I don't know what has become of the original. It was returned to us marked "Cancelled on exchange for refunding bond No. R-2,000, E. O. R., E. Cole, County Treasurer," and I submit that is a sample of the other bonds. Also, we will connect it up with further testimony.

Mr. Crouter: If your Honor please, I would like to examine this for a moment. It has fine printing, and so forth.

The Court: Have you something else you can offer while counsel is examining that?

Mr. Acret: I wonder if we could take a recess? Does your Honor take a recess at midafternoon?



The Court: I think so. We will take a ten minute recess.

(Short recess taken.)

The Court: When we took a recess, counsel for Petitioner had indicated an introduction of some document that Respondent wanted to examine. Is that ready?

Mr. Crouter: Yes, I have examined that, if the Court please, and I have no objection to the document being received in evidence.

The Court: What is the document?

Mr. Acret: It is a photostatic copy of what purports to be one of the cancelled bonds of the first issue, which is marked "Cancelled" in the purported handwriting of the County Treasurer of Yolo County.

The Court: I understand Petitioner is going to connect that as being a copy of one of series of bonds here involved.

Mr. Acret: Yes, and I propose at this time to put Mr. Landrum on the stand.

The Court: The document just marked will be introduced in evidence at Petitioner's Exhibit No. 8.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 8.)

Mr. Acret: Take the stand, Mr. Landrum, please.

The Court: The witness has already been sworn, as [70] I recall.

Mr. Acret: As I recall it, yes.

Whereupon,

ROBERT R. LANDRUM

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Acret:

Q. You were secretary of the Birch Securities Company in 1944?

A. Birch Securities Company—no, 1934.

Q. I will withdraw the question.

You were secretary of the Birch Ranch & Oil Company, were you, in 1944? A. 1944, yes.

Q. When did you first become secretary of the Birch Ranch & Oil Company?

A. I think it was the latter part of 1937.

Q. Were you such from then on continuously up to and including September 30, 1944? A. Yes.

Q. Were you also an officer of the Birch Securities Company during any part of that time?

A. Yes. [71]

Q. When did you first become an officer of the Birch Securities Company?

A. The latter part of '37.

Q. What was that, secretary?

A. Secretary.

Q. Were you secretary of the Birch Securities Company at the time of the receipt of any of the refunded bonds of Reclamation District 2035?

A. Yes.

Q. About when was that, if you recall?

(Testimony of Robert R. Landrum.)

A. I don't know when they were refunded.

Q. Just approximately. The refunding issue is dated January 1, 1935. Did you receive the bonds——

A. Subsequent to that, shortly afterwards, but I don't know the date.

Q. Is it true that for a period in the 1930's the Birch Securities Company was suspended by the Secretary of the State of California?

A. They were suspended—you say in the 30's; sometime after '37.

Q. And by reason of such suspension, was there delay of the Birch Securities Company turning in its old bonds in exchange for the new bonds?

A. Yes.

Q. And such delay was caused by that suspension; that is, [72] such delay as there was in turning in the bonds? A. Yes.

Q. Under the Franchise Tax Statute, you understood it was a misdemeanor for a suspended corporation to transact any business? A. Yes.

Q. And you were advised by your attorney that turning in the bonds would be construed as transacting business? A. Yes.

Q. Did Birch Securities Company finally get an order through the District Court of the United States from the Secretary of State in enjoining suspension? A. Yes.

Q. Did you, sometime subsequent to January 1, 1935, then turn in the old bonds that were owned by the Birch Securities Company for the refunded bonds?

(Testimony of Robert R. Landrum.)

Mr. Crouter: If your Honor please, I must object to this question, on the ground it is leading, and apparently purports to cover things of a documentary evidence nature, concerning which I believe there should be written records which would best show exactly what happened.

The Court: Let counsel refrain from leading the witness.

Mr. Acret: I was doing that in the interest of time, and didn't consider counsel would make any point of it. [73]

Q. (By Mr. Acret): I show you Exhibit No. 7, which is the judgment role of the Superior Court, with reference to the refunded bonds, and I will ask you if the Birch Securities Company received from the county treasury any of the bonds that are listed in this judgment role as R-1 to R-2,000?

A. They received them in exchange for the old bonds of a like amount.

Q. And that was subsequent to January 1, 1935?

A. Yes.

Q. Did you have possession of some of the old bonds, as secretary of the Birch Securities Company?

A. We had a few of them.

Q. You are familiar with their form?

A. Yes.

Q. I will show you a photostatic copy of what purports to be one of the old bonds, which is Petitioner's Exhibit 8 herein, and ask you if that is a sample, this one being No. 2,000, if that is a sample



(Testimony of Robert R. Landrum.)

of one of the original bonds of Reclamation District No. 2035? A. I would say that it is.

Q. It is the issue dated January 1, 1925?

A. Yes.

Q. Are you familiar with Mr. Cole's signature?

A. Yes. [74]

Q. The County Treasurer of Yolo County?

A. Yes.

Q. That is his signature?

A. Yes.

Mr. Acret: I conceive that purports to have kept my promise, your Honor, with connecting up that document.

Q. (By Mr. Acret): During the year 1944, did you receive notices of call from the County Treasurer of Yolo County with respect to the assessment, payment of interest on assessment No. 1 of Reclamation District No. 2035?

Mr. Crouter: If your Honor please, the Respondent respectfully objects to the question at this time, on the ground it is leading and calls for a conclusion, and calls for construction of document by the witness.

Mr. Acret: I will withdraw the question.

Mr. Crouter: I told counsel that with respect to the documents clipped together, I have no objection to their going into evidence for what they show.

Mr. Acret: I wanted to identify it, however.

Q. (By Mr. Acret): Did you receive that instrument entitled, "Notice of Call No. 25 of Assess-

(Testimony of Robert R. Landrum.)

ment No. 1," during the year 1935? A. Yes.

Q. Is that a sample of the instrument which you received [75] from time to time from the County Treasurer with reference to assessment calls?

A. Yes.

Q. In response to that assessment, did you send in the money to the County Treasurer, and for that in return receive that receipt from him in the sum of \$60,769.49, dated September 20, 1944?

A. Yes.

Mr. Acret: We offer the same in evidence at this time, three pages as one Exhibit.

Mr. Crouter: No objection.

The Court: Without objection it is admitted as Petitioner's Exhibit No. 9, three papers attached together, the papers just identified by the witness.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 9.)

Mr. Acret: For your Honor's information, there is a certificate attached from the auditor's office, "This is to certify that Birch Ranch & Oil Company has this day paid into the County Treasurer amounts as follows: Payment of call No. 25 of assessment No. 1 of Reclamation District 2035, \$60,-769.49, dated September 20, 1944, Fred A. Porter, County Auditor, and Roy E. Cole, County Treasurer."

(Testimony of Robert R. Landrum.)

The Court: You just read from the Exhibit, the last document? [76]

Mr. Acret: Yes, your Honor.

The Court: Exhibit No. 9.

Q. (By Mr. Acret): I call your attention to the fact that Exhibit No. 9 is Check No. 618, and referring to Exhibit No. 1, which is the report of the Internal Revenue Agent in charge, dated January 23, 1947, I call your attention to Item No. 4 under "Amounts Allowed" in this report, consisting of four payments in this year by certified checks as follows: Check No. 618, \$60,769.49—is that the same item? [77] A. Yes.

Mr. Acret: That is the fourth item, your Honor, on this page, in this report.

Q. (By Mr. Acret): I now call your attention to Exhibit No. 1, which is again the first report of the Field Agent in charge, page three thereof. I call your attention to an item, check No. 28,553, dated 12-29-43, in the sum of \$64,422.51 for amounts allowed in this report, under the heading "amounts allowed in this report, consisting of four payments in this year by certified checks as follows." Is that a certified check which you sent to the county treasurer? A. Yes.

Q. In return did you receive the receipt there from the county treasurer? A. Yes.

Mr. Acret: We offer the certified check to be received in evidence, the receipt being in form simi-

(Testimony of Robert R. Landrum.)

lar to the first one, except it says, "Receipt in payment of Call No. 23."

The Court: A separate document you are offering?

Mr. Crouter: I have no objection.

Mr. Acret: I am offering the check and receipt together, as one document.

The Court: Are they attached together?

Mr. Acret: I will ask that they be attached. [78]

The Court: They will be admitted without objection as Petitioner's Exhibit No. 10.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 10.)

Q. (By Mr. Acret): Did you receive the Call No. 23 referred to in that receipt? A. Yes.

Q. And paid the item in response to that call?

A. Yes.

Q. That is, that was paid for and on behalf of Birch Ranch and Oil Company?

A. That is right.

Q. I show you now a certified check number 29537, to Roy E. Cole, treasurer, dated January 23, 1944, in the sum of—dated June 26, 1944, in the sum of \$59,093.59. Is your testimony the same with regard to that? A. Yes.

Q. And you received the receipt back from the county treasurer, along with this check that I am showing you? A. Yes.



(Testimony of Robert R. Landrum.)

Q. And that corresponds to item number 2 that is shown on page 3 of the Internal Revenue Agent's first report? A. That's right.

Q. Exhibit No. 1? [79] A. Yes.

Mr. Acret: I offer this in evidence, your Honor.

The Court: One or two papers?

Mr. Acret: Two papers, check and receipt attached.

Mr. Crouter: No objection.

The Court: They will be attached together and marked Petitioner's Exhibit No. 11.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 11.)

Q. (By Mr. Acret): The next item is 37,000, is it? A. Yes.

Mr. Acret: I will put in a photostat of that, if counsel will consent to it. I have shown the other checks heretofore. It is temporarily misplaced.

Mr. Crouter: I have no objection to this check and the related documents being received.

Q. (By Mr. Acret): I show you a photostat of a certified check dated August 11, 1944, number 3601, in the sum of \$37,325.28, payable to Roy E. Cole, treasurer of Yolo County. Did you pay this, together with auditor's receipt to cover a portion of Call No. 21, dated December 5, 1935, together with penalty thereon of Reclamation District No. 2035, did you send that check to the county treas-

(Testimony of Robert R. Landrum.)

urer in behalf of Birch Ranch & Oil [80] Company?  
A. Yes.

Q. To pay the Call referred to in the receipt?

A. Yes, No. 21.

Q. And you suffered a penalty for that payment being late?  
A. Yes.

Q. What did the penalty consist of?

A. I think ten per cent of the amount called; I am not sure.

Q. Why did you only pay the portion of it, if you remember?

A. They made a call for a portion of it, so we paid what they called for. We always pay upon the call, whatever the call is.

Mr. Acet: We offer the photostatic copy of the check and photostatic copy of the receipt as one exhibit.

The Court: That is the document just identified by the witness. It will be received in evidence as Petitioner's Exhibit No. 12.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 12.)

Q. (By Mr. Acet): Mr. Landrum, while you were secretary, did you [81] receive a document entitled, "Report," dated March 23, 1947, from the Internal Revenue Department, of which Exhibit No. 1 I show you is a copy?  
A. Yes.

Q. In reliance on the statements therein contained, "that the Birch Ranch & Oil Company is

(Testimony of Robert R. Landrum.)

held by Judge Turner's decision to be on a cash basis," and in reliance on the fact that your loss that is shown on your income tax return for 1944 was changed from eighty-four thousand odd to one hundred eighty-six thousand odd, did you consult me with reference to your rights with regard to that loss?

Mr. Crouter: If your Honor please, Respondent respectfully objects to the question, on the ground it is leading and suggestive, and that it calls for a conclusion and construction and so forth by the witness, whether he relied, and so forth. I believe he should testify to the facts.

The Court: The question is leading, and I think we might simplify it to eliminate the objection.

Mr. Acret: The question was with respect to that report, as it said so-and-so; did he consult me?

The Witness: Yes, I did.

Q. (By Mr. Acret): What advice did you receive with respect to that item of \$186,000.00?

Mr. Crouter: Did your Honor rule? [82]

The Court: I permitted him to say he did consult counsel.

Q. (By Mr. Acret): Do you understand the question? What advice did you receive from me with respect to that loss of \$186,000.00?

A. The 1941 return was involved at the same time as the 1942, both of which the agent of the Treasury Department claimed there was a tax due, after he had audited those years, 1941 and 1942, and the question was whether we would pay both

(Testimony of Robert R. Landrum.)

of them or not, and you advised, inasmuch as this audit had been made here, just referred to under date of January 28, 1947, that we were on the cash basis. Therefore, we would have nothing to carry back to 1941 from any subsequent year, and that we should pay the 1941 return, relying upon this audit here to wipe out any tax that may be in 1942.

Q. Did you then pay the 1941, on receipt of that advice?      A. We did.

Q. In reliance, as you have stated?

A. Yes.

Q. And that was the amount in the sum of twelve thousand odd dollars?      A. Yes.

Mr. Acret: Take the witness. [83]

#### Cross-Examination

By Mr. Crouter:

Q. Mr. Landrum, were you secretary of Birch Securities continuously down to, what time?

A. Down to date of its dissolution?

Q. What date?

A. Date of dissolution in 1944.

Q. What was the date of dissolution?

Mr. Acret: Just a moment. Unless the date of dissolution is prior to September 30th, it is immaterial here.

The Court: I don't know whether it is prior or subsequent. He asked what was the date of dissolution.

Mr. Acret: If he knows. The certificate would be the best evidence.



(Testimony of Robert R. Landrum.)

The Court: You have reference to the dissolution of what corporation?

Mr. Crouter: Birch Securities Corporation, if he knows.

Mr. Acret: That is objected to as immaterial.

The Court: That is one of the subsidiaries, as I understand it?

Mr. Acret: Well, I don't know as you would call them subsidiary, but it is one of the corporations Mr. Birch controlled.

The Court: I will overrule the objection. I [84] don't know what the purpose of it is.

Mr. Acret: For the sake of brevity, as well as in fairness to us, we are not prepared to meet anything outside of the issues in this case.

The Court: What is the purpose, I will ask Respondent counsel, of this testimony concerning Birch Securities?

Mr. Crouter: Counsel himself brought out that Birch Securities Company was suspended, and I just want to find out how long ago it was suspended, and I believe some of the documents offered by Petitioner with respect to payments, I think that Birch Securities Company is mentioned on some of these, perhaps not, but it seems to me it is material whether there was a corporation operating and doing business during the times these payments are involved.

Mr. Acret: When the Birch Securities Company was liquidated wouldn't have any bearing on any-

(Testimony of Robert R. Landrum.)

thing counsel said, as to when it was suspended. I will stipulate with counsel that the Secretary of State didn't recognize the judgment of the three-judge court, and the Birch Securities Company is still suspended, and we have the matter in the Supreme Court of the United States now. I don't know how far afield we are going to go.

Mr. Crouter: As my recollection serves me, there was definite testimony in here that Birch Securities Company, at the time of turning in certain bonds, did certain things, [85] and this witness did certain things.

The Court: Does Petitioner agree to that statement.

Mr. Acret: That is right, but the question would be to ask him when they turned them in; not when the company was liquidated. That has no bearing on anything that counsel said.

Mr. Crouter: I withdraw the pending question and ask you this,—

Q. (By Mr. Crouter): During the taxable year 1944, who owned the outstanding stock of the Petitioner corporation, Birch Ranch & Oil Company, if you know?      A. The year 1944?

Q. Yes.

Mr. Acret: That is for the fiscal year 1944.

The Witness: Who owned the stock of the Birch Ranch & Oil Company?

Mr. Crouter: That is correct.

The Witness: It depends on what part of the year.

(Testimony of Robert R. Landrum.)

Mr. Acret: The fiscal year.

Q. (By Mr. Crouter): Let's take October 1, 1943. Can you tell the Court at that date who owned all the outstanding stock of the Petitioner corporation?

A. Well, I will have to answer not directly, if I may, [86] because the stock was issued to Mr. and Mrs. Birch and then exchanged for the stock of the Birch Holding Company, was then in the Birch Holding Company.

Q. So that the Birch Holding Company held all of the outstanding stock of Petitioner, is that correct.

A. That is right.

Mr. Acret: Just a moment, if you please.

Well, it covers matters already stipulated to and it is immaterial to any issue in this case. It is our position that if the Birch Ranch & Oil Company owned all the lands and owned all the bonds, it wouldn't make any difference. There is no Higgins-Smith situation here, because under the law of California one person can own both and still avail themselves of the exemption given them by law.

Mr. Crouter: If counsel can show me where the matter is covered by stipulation, I will be glad to reconsider my question, but it is my understanding that the prior findings and the stipulation do not cover the exact situation in 1944.

Mr. Acret: Don't cover the ownership of the three corporations?

Mr. Crouter: Let's check it. It is not my recollection that they do.

(Testimony of Robert R. Landrum.)

Mr. Acret: My understanding was that they did.

The Court: Counsel ought to be able to agree as to [87] what they show.

Mr. Crouter: Let's just check the stipulation. Maybe we can shorten it this way: I will withdraw the pending question. Mr. Acret, do you stipulate here before the Court that during the taxable year 1944, the Petitioner, Birch Ranch & Oil Company, was wholly owned by Mr. A. Otis Birch and his wife, M. Estelle C. Birch, directly, or by them through another corporation?

Mr. Acret: So stipulated, your Honor.

Mr. Crouter: That covers it.

Mr. Acret: Nevertheless, and we will argue it later, that is immaterial. In other words, it is our position that these bonds could be owned by Mr. and Mrs. Birch themselves, and it would make no difference, as they did for 10 years and it made no difference.

The Court: Proceed with the cross-examination. Any other questions of this witness?

Mr. Crouter: Yes, if the Court please.

Q. (By Mr. Crouter): Mr. Landrum, have you brought to Court or could you obtain and show the Court any correspondence between the Petitioner corporation or any of its officers, on the one hand, and Mr. Cole, the Treasurer of Yolo County, on the other hand, with respect to any of these checks which have been received here in evidence and marked Exhibits 9, 10, 11 and 12? [88]

Mr. Acret: I will state to counsel that I have



(Testimony of Robert R. Landrum.)

the correspondence here and will turn it over to him here in open court for his examination.

Q. (By Mr. Crouter): Mr. Landrum, you have handed to me such correspondence as you could find that relates to each one of these four payments concerning which you heretofore testified?

A. Yes.

Mr. Acret: I will turn over three groups. I don't know whether that covers all of them or not.

Q. (By Mr. Crouter): Please examine the various papers your counsel has handed up, and in order to keep the record as orderly as possible, let's take the earliest check in point of time if we can find it here.

Mr. Acret: Could I interrupt a moment? I know that covers it all, because the first one put in had no correspondence in connection with it, and I have given you three groups, and that is all Mr. Landrum has given me.

Mr. Crouter: Very well.

Q. (By Mr. Crouter): Now, Exhibit No. 10 in the case refers to a certain check dated about December 29, 1943. Do you have or can you find any correspondence on or about that date relating to any so-called call or check; if so, just show me the correspondence. [89]

A. What was the amount?

Q. The amount here is \$58,565.92

A. Yes, I have a letter.

Mr. Acret: I am giving this to counsel, your Honor, so there won't be any question of our good

(Testimony of Robert R. Landrum.)

faith. Nevertheless, when he produces the correspondence, I will object to it as immaterial. He can see all the correspondence he wants to, but it doesn't make any difference what it is, the Treasurer sends his call in compliance with the law.

Q. (By Mr. Crouter): You have shown me a letter dated December 18, 1943,—

The Court: From whom to whom?

Mr. Crouter: This is to the Birch Ranch & Oil Company from Roy E. Cole, Treasurer of Yolo County.

Q. (By Mr. Crouter): Is this the only communication you can find on or about that date, or the only one you have found?

A. I don't seem to have any that pertains to that, other than that letter.

Q. Did you find any copy of a letter, any letter, from the Birch Ranch & Oil Company or any officer of that company to the Treasurer of Yolo County, on or about that date or just before that date?

A. I have a letter here dated December 28, 1943, to [90] Roy E. Cole from Birch Securities Company.

Q. May I see that?

A. I don't think it refers to that particular item.

Q. It does not refer to any of that same matter. Very well, I just wanted to be certain we have all the correspondence.

A. No, that doesn't have any reference to that.

(Testimony of Robert R. Landrum.)

Mr. Crouter: If your Honor please, Respondent at this time offers in evidence the letter identified by the witness dated December 18, 1943.

The Court: Any objection?

Mr. Acret: No objection.

The Court: It will be admitted as Respondent's Exhibit No. B.

(The document above referred to was received in evidence and marked Respondent's Exhibit B.)

Q. (By Mr. Crouter): Now, Mr. Landrum, Exhibit No. 11 in the case refers to a check dated June 26, 1944. Please examine your papers and see whether you have any correspondence at all relating to any check for about \$53,721.65.

Mr. Acret: May it be understood, counsel, you are asking the witness to refer to papers which we have produced here ourselves?

Mr. Crouter: Pursuant to my request.

Mr. Acret: Pursuant to your request just made here [91] in court.

Mr. Crouter: And previously, also.

Mr. Acret: Made to me orally; that is correct.

Mr. Crouter: Yes.

Mr. Acret: In other words, I told you I would do so, produce what correspondence we had, and so far as I know, we have done it.

The Witness: I have some correspondence here relating to that payment.

Q. (By Mr. Crouter): You are showing me

(Testimony of Robert R. Landrum.)

certain letters, originals, and one copy, five documents, all clipped together, and these apparently start about April 10. In fact, the first one is dated April 10, 1944, and the last one is dated June 13, 1944. I offer these, if the Court please.

Mr. Acret: Will you show them to me, first

Mr. Crouter: In the meantime, please look at the other two exhibits and see if there is any correspondence relating to Exhibit No. 9 and Exhibit No. 12.

Mr. Acret: No objection to this offer, your Honor.

The Court: Let the document be formally presented for admission, and also tell what it is, so it can be designated properly.

Mr. Crouter: For the record, if the Court please, this is a group of five original letters, a copy of a statement, and an original of a document from the—well, it is labeled “Woodland Democrats, Ed E. Leak Publishing Company, Woodland, California.” It appears to be a statement of some [93] kind.

This is an original dated April 10, 1944, a copy of a letter from Petitioner——

The Court: Are you offering these all as one exhibit?

Mr. Crouter: Yes, I am.

—— a copy of a letter dated April 14, 1944, original of a letter from Mr. Cole to the Petitioner, dated April 19, 1944; an original of a letter from Mr. Cole to the Petitioner dated April 12, 1944, and



(Testimony of Robert R. Landrum.)

an original letter from Mr. Cole to the Petitioner dated June 13, 1944.

The Court: How many sheets of paper are contained?

Mr. Crouter: Five, altogether.

The Court: The five sheets just enumerated by Respondent's counsel will be admitted in evidence as Respondent's Exhibit No. C.

(The documents above referred to were received in evidence and marked Respondent's Exhibit No. C.)

Mr. Acret: Counsel, could I interrupt you a minute. During the recess, you submitted to me about putting in the tax return for 1942. I suggest we do that at this time, before the close of the day, so we won't forget it.

Mr. Crouter: I have it on my table. I will be glad to. [94]

Mr. Acret: Will you remember it?

Mr. Crouter: You see that I don't overlook it?

Mr. Acret: I suggest we offer it, put it in right now, while we think of it.

Mr. Crouter: If that is agreeable to the Court.

The Court: It will be admitted as Joint Exhibit—

Mr. Crouter: If your Honor please, that does break up our sequence relating to the other matters.

The Court: All right. Proceed with the examination of the witness.

Q. (By Mr. Crouter): Mr. Landrum, the next

(Testimony of Robert R. Landrum.)

group of letters relating to the next check, please.

A. A package of letters, various of them, starting with——

Q. Can you tell me how many originals or copies and how many letters are all clipped together?

A. Three original letters, that is, three original letters from R. E. Cole, Treasurer of Yolo County.

Q. And two retained copies?

A. And three copies of letters written to Roy E. Cole, County Treasurer, by Birch Ranch & Oil Company, and attached to it——

Mr. Acet: That has been put in, the photostat was put in.

The Witness: There is a receipt from the [95] County Auditor, in the amount of \$37,225.28.

Q. Just to make it short, the first two pages are the originals of Exhibit No. 12 in evidence, are they not? A. That is right.

Mr. Acet: They should be taken off then, so there is no duplication.

Mr. Crouter: At this time the Respondent offers the six letters identified by the witness, and I agree the originals of the others may be removed by counsel, since the photostats are already in evidence.

Mr. Acet: It would be to the Petitioner's advantage if your Honor were reading these and getting the impression of these, the effect of these, as they go in evidence. I know it will be the same in the end. These are quite interesting.

The Court: I would rather read them all at once. They will be admitted. How many sheets are there?

(Testimony of Robert R. Landrum.)

Mr. Crouter: Six different pages.

The Court: All attached together?

Mr. Crouter: That is correct.

The Court: They have just been enumerated by Respondent's counsel, and will be admitted as Respondent's Exhibit No. D.

(The documents above referred to were received in evidence and marked Respondent's Exhibit No. D.) [96]

Q. (By Mr. Crouter): Now, Mr. Landrum, referring to our next check here as shown by Exhibit 9 in evidence, and the date on or about September 20, 1944, do you have any correspondence relating to that matter? A. I do not.

Q. None whatever?

A. None for that, but I have some correspondence here relating to Call No. 23, if you can locate that Call No., as shown on the receipts.

Q. What is the date of the letter that refers to such call? Let's see if it is within our taxable period, what is the date?

A. November '43, December '43; November and December.

Mr. Acet: That relates to other matters.

The Witness: I don't think you have Call No. 23 among those. I am not sure.

Q. (By Mr. Crouter): Does this group of letters, all clipped together, relate to the same subject matter?

(Testimony of Robert R. Landrum.)

A. Apparently so.

The Court: What subject matter does it relate to, anything that has been introduced?

Mr. Acret: I am going to object to it as immaterial and not related to any matters he elicited from the witness, [97] and the examination in chief, and has nothing to do with any issues. It is just cluttering up the record.

Mr. Crouter: If your Honor please, the first letter is an original from the Treasurer to the Petitioner, relating to Call No. 23, dated October 18, 1943; the last copy of a letter from the Birch Securities Company to Mr. Cole, dated December 28, 1943, and they purport to relate to certain calls and payments with respect to reclamation bonds.

The Court: All relating to Call 23 or other calls?

Mr. Crouter: They are not all identified, if your Honor please, but by amounts and figures, they might trace through.

The Court: Is Call No. 23 identified by any check that has been offered here? Is that another call?

Mr. Acret: Your Honor, I am going to withdraw my objection, for the reason that this is illustrative of the general process which is followed, and it will be helpful to the Court.

Mr. Crouter: Thank you.

The Court: It may be introduced as Respondent's Exhibit No. E. How many pages are there, so we can know what it is.

Mr. Crouter: This consists of three original let-



(Testimony of Robert R. Landrum.)

ters from Mr. Cole to the Petitioner, and four copies of letters, three of which are from the Petitioner to Mr. Cole, and the [98] last one, December 28, 1943, is from Birch Securities Company to Mr. Cole.

The Court: They will all be admitted as one exhibit, Exhibit E.

(The documents above referred to were received in evidence and marked Respondent's Exhibit No. E.)

Mr. Acret: If I may be permitted to state, this will be helpful to your Honor, in that the first page illustrates the matter that I said we would show in my opening statement, and in that I called your Honor's attention to the fact that the Reclamation Act provides for the buying of interest coupons and turning the coupons in as payment, in exchange for the county treasurer paying for them. It just illustrates the process, as I stated it would, in my opening statement. That may be helpful two months from now when you read the transcript.

Q. (By Mr. Crouter): Mr. Landrum, please tell the Court what usually determined the date that Mr. Cole, the county treasurer, would make a demand of the Petitioner for any payment of money, and—I will stop right there. What usually determined that?

Mr. Acret: Just a moment, please. That is objected to as calling for something he can't tell, what determined [99] a third party to do something, and

(Testimony of Robert R. Landrum.)

further than that, it is obvious what determines it. It is what the law of California is.

The Court: If the witness knows, he can say.

The Witness: I do not know.

Q. (By Mr. Crouter): Referring to Exhibit B, this being a letter from Mr. Cole to Birch Ranch and Oil, dated December 18, 1943, and the last paragraph reading as follows: "I will appreciate a letter from you, so that I may know what to expect in the matter of business connected with District No. 2035."

I will ask you first, did you usually receive communications from Mr. Cole and act for the company?

A. No, sir, I never did. I didn't even answer that, that I know of. I couldn't.

Q. Then you had nothing whatever to do with the question of issuance of any checks to the County Treasurer. Is that your testimony?

A. That is my testimony. I couldn't tell him what to do.

Mr. Acret: Excuse me. I think the witness misunderstood the question.

Mr. Crouter: I thought he answered it.

The Witness: I said I couldn't tell the county treasurer what to do, even though he would ask me. I could suggest something, but I certainly couldn't order him. [100]

Q. (By Mr. Crouter): During 1943 and 1944, did you work for the Birch Ranch and Oil Company? A. Yes.

(Testimony of Robert R. Landrum.)

Q. What was your position?

A. Secretary.

Q. Did you handle any correspondence at all for and on behalf of the corporation? A. Yes.

Q. Did you handle any correspondence with Mr. Cole, the treasurer of Yolo county?

A. Yes, I did.

Mr. Acret: Just a moment. This is objected to as argumentative. The witness has just identified all the correspondence and now counsel is asking him if he handled that.

The Court: I assume it is introductory to some other question.

Q. (By Mr. Crouter): Did you receive any of these letters which we have identified here from Mr. Cole, on behalf of the corporation? Did you receive them and do anything with them?

A. I suppose we did. You have got them there before you.

Q. I mean, did you act for the corporation, or did some one else handle all this? [101]

A. If I had any letters there, I handled them. How are the letters signed, secretary?

Q. Well, this one, Exhibit C, has no initials, but I am referring to the letter of April 14, 1944, and it is signed "Birch Ranch and Oil Company, by . . . . . " and "Secretary" below.

A. I must have signed it.

Q. Were you the only secretary at the time?

A. I don't know just what you mean. There is only one secretary of a corporation.

(Testimony of Robert R. Landrum.)

Q. And you usually signed mail for the corporation, when the secretary signed them?

A. Yes.

Q. Now, this letter I referred to of April 14, refers to reconciling certain figures. Does that just refer to totals of payment to the county, or does that refer to payments from the county also?

A. From the county—I don't know what you mean.

Q. I believe you stated you don't know.

A. I don't know what you mean.

Q. Referring to the second inset paragraph where it states, "To cover interest coupons submitted for payment, \$120,000.00." I will ask you this: Please tell the Court whether it was the practice to make a payment to the treasurer from the corporation or on behalf of the corporation, and about the same time interest coupons would be clipped from bonds and presented to the county treasurer, and the treasurer would also make a payment to the Birch Ranch and Oil Company, or to Mr. Birch, individually?

Mr. Acret: Just a moment. That is objected to as multiple, and I don't think the treasurer would make a payment to the Birch Ranch and Oil Company.

Mr. Crouter: I said, "or Mr. Birch, individually."

Mr. Acret: You don't mean to Birch Ranch and Oil Company. Objection; question multiple.

Q. (By Mr. Crouter): And make a payment to Mr. Birch individually?



(Testimony of Robert R. Landrum.)

Mr. Acret: Objection now. The question is understandable.

The Court: If the witness understands, answer the question.

The Witness: No, sir, I do not understand the question.

The Court: Will counsel kindly restate it.

Mr. Crouter: I withdraw the pending question.

Q. (By Mr. Crouter): Please tell the Court whether on any occasion, during the fiscal year 1944, there was a payment made to the county treasurer by and on behalf of the Petitioner corporation, and about the same time, we will say, within a few days, at least, [103] there would be a payment of approximately the same amount from the county treasurer to Mr. Birch or to someone on his behalf?

Mr. Acret: Just a moment. That is objected to as immaterial and multiple.

The Court: I will overrule the objection. Will the witness answer the question, if he knows.

The Witness: I don't know all the ramifications of the county treasurer's office, or how he does things, or how Mr. Birch handles his matters. Those coupons are out of my jurisdiction entirely. I am merely referring in this letter here to the calculations, how he arrived at certain figures, but I don't have anything to do with the coupons.

Q. (By Mr. Crouter): Do you know whether any coupons were presented to the county treasurer at any time for payment of any interest on those coupons and redeeming the coupons, turning them

(Testimony of Robert R. Landrum.)

back to the treasurer, during the fiscal year 1944?

A. Yes. First, let me say that all of these bonds that were owned by the Birch Securities Company were in a trust at the Citizens National Trust and Savings Bank, as security, under an agreement that Mr. Birch had with the Hopkins sisters, so-called, so at any time there was a call being made by Mr. Cole, when the call was made, I will say, those coupons had to be clipped from those bonds by the trustees of that trust. Mr. Frank B. Olds was one of the trustees, and C. Harold Hopkins [104] was the other trustee. They would go down to the bank, clip the coupons, and send them up to Mr. Cole. Sometimes they would remain there until he made a call, so they would be on hand. Mr. Hopkins wasn't always available. He traveled around. So about the time an interest was due, a payment for interest, he would clip these coupons off and send them up there, and Mr. Cole would keep them in a safe securely there.

Th Court: Who would clip them off?

The Witness: The trustees of this trust.

The Court: That is at the bank?

The Witness: Yes, sir. That is about all I can explain about that.

Q. (By Mr. Crouter): Was it the usual practice that about the time of a payment from the Petitioner corporation to the treasurer, there would be a similar payment from the county treasurer to anyone who presented the bond coupons?

Mr. Acret: Just a moment. That is objected

(Testimony of Robert R. Landrum.)

to as immaterial, calls for a conclusion, and not the best evidence.

Mr. Crouter: I am just asking insofar as he knows.

Mr. Acret: I think he already said he didn't know.

The Witness: So far as the county treasurer is concerned, he wouldn't hold the money any longer than he had to. If he had the money, he would pay it upon the presentation of the coupons, no matter who presented them. [105]

Q. (By Mr. Crouter): Please tell the Court whether it was the practice, during the fiscal year 1944, and it did happen there with four payments from the county treasurer, on the bond coupons, in almost the same amount that was paid to the treasurer. In other words, the record here indicates that the four checks in evidence seem to total \$221,-610.87. Please tell the Court, if you know, whether approximately the same amount was paid out on bond coupons during that fiscal year and at about the same time of the payments that were made to the treasurer.

Mr. Acret: Your Honor, that is calling for a witness' guess. How could a man other than guess?

The Court: He either knows or he doesn't know. If he knows, he can say so; if he doesn't know, he can say so.

The Witness: I would have to verify those figures. I couldn't answer right off.

(Testimony of Robert R. Landrum.)

The Court: You would have to verify them, you say?

The Witness: Yes.

The Court: How long would it take?

The Witness: He has all my correspondence there, for one thing.

The Court: The witness says he can't do it without verification. [106]

Q. (By Mr. Crouter): Are there any books or records available in court that you could consult and answer the question?

A. As I said before, I have nothing to do with the coupons. I can show you how much was paid.

Q. Did you keep any records at all with respect to amounts paid on bond coupons?

A. I surely do.

Q. Do you have any such records available in Court?      A. Yes.

Q. Will you please consult such records, so we can examine and see what was done?

The Court: We will take a five-minute recess while the witness is making an examination.

(Short recess taken.)

The Court: Mr. Landrum, resume the stand, please.

Q. (By Mr. Crouter): Did you find any record with respect to amounts of interest received from the county?

A. No, sir. I misunderstood the question before. I remember some, however.

Q. Please tell the Court what you remember, if



(Testimony of Robert R. Landrum.)

anything, that transpired with respect to that matter during the fiscal year 1944, and if you care to refer to——

A. The Birch Ranch and Oil Company bought 86 of those bonds from the Great Republic Life Insurance Company, who [107] owned them at that time. The Birch Ranch and Oil Company purchased them in 1940. Those bonds had some back interest on them, and we acquired that back interest, and subsequent to buying them, and at the time, or soon after, let's see—1943, we started paying taxes to the county treasurer, upon his calls. The Birch Ranch and Oil Company, owning the 86 bonds, they would present those coupons for payment. Now, that interest is on the books, but I don't have it with me here.

Q. Mr. Landrum, is there any complete list or is there any definite written evidence that you could refer to here, so that you could tell the Court the exact situation as to what, if any, bonds were outstanding, that is, bonds in the reclamation district, during the fiscal year 1944, and who held those bonds?

A. I don't believe I can do that, even if the papers were presented to me. It is a very complicated matter.

Mr. Acet: I would like to state to counsel and your Honor that Mr. Birch is going to take the stand, and he is familiar with that situation.

Mr. Crouter: It will be shown by him?

(Testimony of Robert R. Landrum.)

Mr. Acret: He will be able to so testify, I believe.

Q. (By Mr. Crouter): Now, Mr. Landrum, referring back again to Exhibit C in evidence, I call your attention to the third paragraph of [108] this letter from Mr. Cole, which is addressed to Birch Ranch and Oil Company, June 13, 1944, and I read as follows: "If this call remains unpaid, we will be unable to pay interest coupons due July 1st."

Now, does that refresh your recollection at all as to how those matters were usually handled, so you can tell the Court any more about it?

Mr. Acret: I think the letter speaks for itself.

The Court: Well, counsel is asking him if he can refresh his recollection on some previous question. I will overrule the objection.

The Witness: I don't know what he has reference to, other than what he says. He says it can't be paid. If you don't pay the assessment—he couldn't pay the coupon unless we paid our assessment.

Q. Is that what a coupon payment by the county treasurer usually depends upon?

A. It depended on the interest on the call to pay.

Q. If he did not have money on hand, that had been received from these calls, he would not have money to pay the interest. Is that the way it works?

A. Yes, sir.

Q. And sometimes would there be amounts, I mean, coupons, which could have been presented

(Testimony of Robert R. Landrum.)

but they were not presented or paid, because the county treasurer had no money from these calls?

A. If they presented it and he had no money, he couldn't pay them.

Q. Did that ever happen, that you know of?

A. Not to my particular knowledge right at the moment. I don't know of any case.

Q. Now, referring to the second letter in Exhibit C, reading as follows—this is a letter, if the Court please, from Mr. Cole to the Petitioner, dated April 12, 1944, and reads: "This call is for \$53,721.65, which sum, together with the balance on hand, will be sufficient for the payment of sixty thousand dollars coupons due July 1st. As a matter of fact, there will be a remainder over after payment of the sixty thousand dollars."

Now, after seeing that, please tell the Court whether it is correct that it was the usual practice to collect a certain amount from the Birch Ranch and Oil Company, and then pay out either the identical amount or substantially the same amount on bond coupons?

Mr. Acret: I object to this witness testifying what is the usual practice of the county treasurer.

The Court: I will overrule the objection. If the witness knows, he ought to tell.

The Witness: I will answer that by saying that the county treasurer is guided by certain rules in calculating the amount of calls that he is to make. It is never for the same [110] amount as the interest. It is a very complicated system, and in one

(Testimony of Robert R. Landrum.)

of the exhibits you now have, he explains just how that call is made and how it is calculated. That is the thing I was trying to find out about in some of the correspondence I had with him. That is what he has reference to in this paragraph you just read. He always has a certain amount left over to carry on to the next call. It is always a few thousand dollars, but that is the way the law requires him to calculate these calls. He can't deviate from that.

Q. (By Mr. Crouter): Please tell the Court whether it is true that no amounts would be paid on interest unless they had been previously collected on these calls. A. That is correct.

Mr. Acet: I object. Already asked and answered.

The Court: He has answered that. For the second time, he has answered that.

Q. (By Mr. Crouter): And that same thing is shown—first, I will ask you, did you dictate and send the first letter here of December 28, 1943, in Exhibit E? A. Yes.

Q. And that is the same matter you referred to when, in the last paragraph, where you state: "Where funds are available, will you please redeem the above numbered coupons, together [111] with the twelve seventy-eight to be delivered to you by Mr. Hopkins," and so forth?

A. That is right.

Q. As a matter of fact, sometimes the payment of any money to the county treasurer by the Peti-



(Testimony of Robert R. Landrum.)

tioner was conditioned upon the payment of interest on coupons at or about the same time, isn't that a fact, as shown by paragraph two of your letter of August 3, 1944, which is Exhibit D?

Mr. Acret: That is objected to as calling for a conclusion of the witness; argumentative.

The Court: Objection sustained. That is just a repetition of what has already been said. If it is not in evidence, I will admit it, but the Court understood that he had answered.

Q. (By Mr. Crouter): Referring to your testimony that the Birch Securities Company was suspended at the time of certain refunding of bonds, what time did you refer to, 1935?

A. I wasn't here in 1935. I don't know——

Q. As I recall, you were asked whether the Birch Securities Company, at the time of the turning in and receipt of any refunding bonds, was suspended. Didn't you answer yes?

Mr. Acret: I don't think that is the question.

The Witness: Yes, but the suspension took place after 1935. [112]

Q. (By Mr. Crouter): How long was it suspended?

A. Sometime after '37. It was suspended after '37, I believe.

Q. How long did it remain suspended?

A. Still is, so far as I know.

Q. Then, the Birch Securities Company was suspended from operations during all of the taxable year 1944?

A. It was dissolved in 1944.

(Testimony of Robert R. Landrum.)

Mr. Acret: I object to the witness volunteering. The dissolution has nothing to do with it, and is outside the fiscal year of 1944.

The Court: I will overrule the objection. If he knows when it was suspended, he can say.

The Witness: I don't know exactly when it was suspended.

Q. (By Mr. Crouter): Do you know whether Birch Securities Company was in existence at all during the tax year 1944, as an active corporation, licensed to do business?

Mr. Acret: Could I hear the question?

(The question was read.)

Mr. Acret: That is objected to as calling for a conclusion; immaterial.

The Court: Do you know whether that is true or not? [113]

The Witness: That is a legal question. I would rather not answer it.

The Court: You don't know what steps had been taken toward its dissolution at that time, then?

The Witness: I know that we went through the process of dissolving it. As to the legality of it, that is not for me to answer.

The Court: The witness can't answer that.

Q. (By Mr. Crouter): Did the question of suspension of that corporation have anything to do with the refunding of any bonds of the Reclamation District or the holding up of any refunding of any such bonds?

(Testimony of Robert R. Landrum.)

A. Not to my knowledge.

Mr. Acret: I may have mislead counsel on that. I was mistaken. I thought at the time when I asked the question I did that was the case, but I recall now that the auditors held it up. I will ask the witness on redirect examination some further questions on that subject.

Q. (By Mr. Crouter): The cause of suspension was on account of certain tax claims made by the State of California, isn't that right? The company refused to pay them?

A. You mean, the suspension was?

Q. Yes. [114]

Mr. Acret: Do you want a stipulation on that? I will make an offer. I offer to stipulate that the Birch Securities Company was suspended sometime, I think, commencing as late as 1939, probably, on the ground of nonpayment of a deficiency assessment, and took the position, and has ever since taken the position, it wasn't subject to the jurisdiction of the State Franchise Tax Commissioner, because it isn't doing business in California. That was being litigated before the Supreme Court.

Mr. Crouter: I appreciate counsel's stipulation, but I know nothing about it, so I can't stipulate. Thank you very much.

Q. (By Mr. Crouter): Referring to Exhibit 4 in evidence, this being the collector's receipt for a payment of \$12,398.85. You do not know of any assessment of that tax against the corporation for

(Testimony of Robert R. Landrum.)

that year, do you? Has there been any assessment you know of?

Mr. Acret: That is objected to as immaterial, argumentative and understandable. What would an assessment against the corporation have to do with this witness paying a deficiency assessment made by the Collector of Internal Revenue in order to conform with his report?

The Court: If the witness knows, he can say so. If he doesn't know, he can say so. [115]

The Witness: The receipt calls for taxes for the fiscal year September 30, 1941. I went up and paid it myself.

Q. (By Mr. Crouter): Did you ever receive a notice and demand from the collector for that year, and with respect to that identical amount?

A. I paid what they asked for, your Treasury Department, and it was for the year 1941. It was right after leaving this court room.

Q. Was there any conversation about that amount being held in a suspense account by the collector; I will say a suspense account, pending the outcome of this case?

A. That is something I can't answer.

Q. I am asking you, was there conversation?

A. I don't know.

Q. Did you, yourself, handle it or turn it in?

A. I was told by our attorney to go up and pay the 1941 taxes, and I did.

Q. Did you come in personally?



(Testimony of Robert R. Landrum.)

A. I went right down there and paid it and got the receipt.

Q. To the collector's office?

A. In this building somewhere.

Mr. Crouter: My only point on that, if the Court please, this relates to the estoppel question, and will take [116] notice of the fact that no decision has been entered and the law will prohibit assessment. I merely wanted to show the status of the twelve thousand dollars at this time. I offer a certificate for the collector of this district, referring to the status of all assessments and collections of the Birch Ranch and Oil Company for all years, 1934 through 1947.

Mr. Acret: Your Honor, with respect to paying this assessment, deficiency assessment is set up as an Exhibit A to the Petitioner herein, and certainly can't have any bearing on the question of estoppel, when we find out, after we file the petition, that Judge Turner's decision, and that the commissioner takes the position we are on a cash basis, and then if we are generous enough to say we have no opposition and this petition isn't taken properly then, if they are on a cash basis, we didn't pay it and we will go pay it now. The question of the estoppel still comes in. We paid it in reliance on this position taken in the first report.

Mr. Crouter: If your Honor please, I would merely like to say—I am not trying to foreclose Petitioner in any respect on the question of estoppel, but I am trying to furnish the Court and have

(Testimony of Robert R. Landrum.)

in the record the exact status of the collector's account with respect to that matter, so it will be fully and clearly evident.

The Court: Whatever the witness knows about, he can tell. [117]

Mr. Crouter: Well, the document offered is a certificate signed by the collector, original certificate, usual certificate of assessments and collections, and the Court can see what is shown here.

The Court: Has that been offered?

Mr. Crouter: That is pending offer now.

The Court: If the witness knows anything about it, he can testify about it, identify it. It seems to be a statement from the Collector of Internal Revenue. Let counsel look at it.

Mr. Acret: It is objected to as immaterial and hearsay and irrelevant.

The Court: Does the witness know anything about this document? That is what the Court wants to know.

The Witness: I have never seen that document.

The Court: Let the witness see what we are talking about.

Q. (By Mr. Crouter): I show you what purports to be an original certificate of the Collector of Internal Revenue for the Sixth District of California, Form Eight Ninety-nine, and I call your attention to the year, fiscal year 1941, as shown on this certificate, together with certain things as to other years, and ask you whether this refreshes your recollection at all as to whether there has been

(Testimony of Robert R. Landrum.)

any actual assessment of the twelve thousand odd taxes for the year 1941?

Mr. Acret: That is objected to as argumentative, your Honor. This proceeding is in response to the assessment for the year 1941, and it is set up as Exhibit A——

The Court: I don't know what the witness knows about it. He has been asked whether he knows about it. If you do, say so.

The Witness: I have never seen this before, and still don't know what it is.

Mr. Crouter: I offer it as an original. Will the Court take judicial notice of the fact that Harry C. Westover is the duly constituted collector of this district, and this is an original certificate over his written signature, with respect to the status of Petitioner's account. I offer this for 1941, to show that exact matter, and offer it also as to all years, in support of the Respondent's position.

The Court: What is the date of this payment made, shown in Exhibit 4?

The Witness: July 7, 1947.

Mr. Acret: In the Commissioner's report, your Honor, showing the loss, was January, 1947, and this assessment that we paid was made under a letter of April 30, 1945.

The Court: This document now before us, dated October 15, 1948, I think counsel had better wait until his testimony to offer this. The witness knows nothing about it. [119]

(Testimony of Robert R. Landrum.)

Mr. Crouter: Very Well.

Q. (By Mr. Crouter): Mr. Landrum, in accordance with your discussion with Mr. Acret and at about the time the amount of the 1941 tax was paid, what, if any, reason was there for not paying the 1942 taxes at the same time?

A. Based upon the audit of the field agent of the Treasury Department, saying we were on a cash basis, and he having found our deductions to be what we had already placed there, and added more to it, so, assuming that we had \$186,000.00 loss, we presumed we could carry that back and wipe out the 1942.

Q. Was there any discussion with Mr. Acret as to the year 1941 still being in the pending docket number, so that any rights of the Petitioner could be investigated before the Tax Court, regardless of the question, whether it was paid or not?

A. No, we knew we had to pay that and wanted to pay the interest on it.

Mr. Acret: Your Honor, I am astonished and surprised that when counsel here corroborates with my opponent to the extent—the minute I find out we don't have a case in any respect, I advise my client to pay the bill, and then have the government complain of it. I do that because I feel it is my duty as a lawyer to no longer make any contentions I don't think I can sustain. We do that and pay that and now [120] counsel wants to take the position as though we had done something wrong. As an honorable gentleman, I say, as to



(Testimony of Robert R. Landrum.)

1941, if we are on a cash basis, our position isn't sustainable, and we give up, so there will be no mistake about it. That is what we did, and paid the bill, and if it is ever found we owe it, we will pay it promptly, and we are well able to, but we don't think, under the law, we are required.

Q. (By Mr. Crouter): Mr. Landrum, from what source and what is the earliest date you knew anything about who the bondholders were of Reclamation District 2035. I refer to these documents you have identified in part, Exhibit No. 5 and Exhibit 6 and Exhibit 7, which seem to relate to certain court proceedings in Yolo County, California?

Mr. Acret: I didn't put Mr. Landrum on with regard to that or ask him anything with regard to it, and counsel is losing time.

The Court: I believe counsel for Petitioner stated that Mr. Birch will cover that?

Mr. Acret: That is right.

The Court: So, counsel, I think you might reserve that examination for him. He can give it more definitely, as I understand it.

Mr. Crouter: If your Honor please, I want to stay within the Court's ruling here, but according to my notes, [121] Exhibit No. 7 was shown to this witness, and there was certain testimony about it. Exhibit 7 relates to certain alleged refunding of bonds, and so forth, and there was testimony about it, and I would like to interrogate on cross-examination about it.

The Court: Anything that pertains to that, the

(Testimony of Robert R. Landrum.)

witness was asked about, but going into the question of ownership of bonds was a matter this witness could give you more accurate information concerning.

Q. (By Mr. Crouter): Referring to Exhibit No. 7, Mr. Landrum, this is the same document which, according to my notes and recollection, you examined when Mr. Acret was asking you questions, and referring to certain alleged refunding of bonds, please tell the Court, in the first place, who handled the originals of records of the reclamation district, and with respect to refunding of bonds, if you know.

A. Our attorneys at that time were Armfield and Eddy, in Woodland, California. He handled all those matters, and I recognize this document here as being connected with that transaction. That is about as far as I can testify to it.

Q. Exhibit 7 has, on the first page, what apparently is the last entry in the proceeding, the very next page showing that the complaint was filed, and filed April 26, 1935. Then, on April—no, on June 25, 1935, there was an order apparently [122] entered by Mr. Harry R. Saunders, clerk of the Superior Court of Yolo County. Now, that date, June 25, 1935, was before you had any connection with any of the Birch corporations, wasn't it?

A. Yes, sir.

Q. Then, please tell the Court whether it is a fact that you, yourself, do not know anything about

(Testimony of Robert R. Landrum.)

there having been any reissuance of bonds of Reclamation District No. 2035 sometime in 1935?

A. I know there was, and this is a certified copy of the document, which was asked for in a previous case.

Q. You just know what is shown by that document?

A. No, I know the bonds were refunded in a subsequent year to '35.

This is a refund—this is a refunding issue, isn't it?

Q. The matter in there refers to refunding of bonds.

A. Well, we had to have this in another case in this court here.

Q. Were you an officer at any time of Reclamation District 2035?      A. Yes.

Q. What was your position with respect to that district?

A. One of the trustees in the latter years.

Q. During what years? [123]

A. I don't remember off hand. I think it was subsequent to 1937 or 1938.

Q. Do you remember whether you were an officer of the reclamation district at any time during the tax year 1944?

A. I think I was. I am not sure. All those matters were handled by our attorneys up there in Woodland, but I think I was.

Q. Armfield and Eddy or Eddy and Armfield?

A. Armfield and Eddy, they called it.

(Testimony of Robert R. Landrum.)

Q. Have you, as an officer of the reclamation district, brought any records of the reclamation district to this court?      A. No.

Mr. Acret: I will object to that question, and I would like to ask a question on voir dire, if that can be asked; I don't know, because I forget, with reference to one's own witness. It is not shown that this witness is an officer of the reclamation district now, and he wouldn't have any authority to bring any records here, and it is not known he is subpoenaed to bring any here or that he has any in his possession.

Mr. Crouter: Well, the question has been asked and answered. I have nothing further.

Mr. Acret: He said he doesn't know; he might have been in 1944. I was trying to get my objection in before the witness answered. I don't want him placed in the position as [124] though he had to bring records here that were not subpoenaed.

Q. (By Mr. Crouter): Can you tell the Court, from your own knowledge, Mr. Landrum, who, if any, were the other trustees of the reclamation district during the tax year 1944?

A. I don't know until I refer to the records. There was very little transactions made in the district at that time, so I don't know.

Mr. Crouter: No further questions. Thank you.

The Court: Any further questions by Petitioner of this witness?

Mr. Acret: I have one or two on redirect.



(Testimony of Robert R. Landrum.)

Redirect Examination

By Mr. Acret:

Q. Counsel asked you if it ever happened that coupons were presented and not paid, and you stated you didn't recall. I want to ask you now if this will recall anything to your recollection: Do you know why the Birch Ranch and Oil Company bought the Great Republic Life Insurance bonds?

A. Yes, I know why.

Q. What was the reason?

A. Because we were sued by the Great Republic Life for payment of those bonds, and if we didn't pay them, they were going to foreclose on the land.

Q. As a matter of fact, do you know what the suit was? [125]

A. The suit was to foreclose.

Q. The Great Republic started foreclosure of the bonds? A. Yes.

Q. Do you know of coupons that were presented to the county treasurer and weren't paid?

A. By the Great Republic Life?

Q. Yes.

A. Yes, they presented them.

Q. That is what happened, when they weren't paid——

A. I thought he meant, did I know of any in our particular family here, and I didn't.

Q. That is what happened, when the bonds

(Testimony of Robert R. Landrum.)

weren't paid, the whole issue was foreclosed. Is that right?      A. That is right.

Recross-Examination

By Mr. Crouter:

Q. Do you know of a long period of time prior to 1944, when, for some years, there were no payments, but there were no foreclosures?

Mr. Acet: That is immaterial. There were lots of time extended, your Honor, to everybody during the depression, and that doesn't indicate anything, any skullduggery.

The Court: The witness can answer if he knows what the answer is.

Mr. Crouter: What was the answer? [126]

The Witness: What was the question?

(The question was read.)

The Witness: Insofar as the Great Republic Life was concerned, they later liquidated or sold out to the Postal Union Life Insurance Company, and as soon as the Postal Union acquired the 86 bonds they were constantly demanding payment, which we kept stalling off from time to time. We did not have any money to buy them with at that time, so we kept stalling them off until finally they got impatient and sued us.

Q. (By Mr. Crouter): Mr. Landrum, please tell the Court whether it is a fact that between June 30, 1933, and about December 29, 1943, during that whole interval of time, from 1933 to that

(Testimony of Robert R. Landrum.)

date in 1942, there were no payments whatever made by the Birch Ranch and Oil Company to the county treasurer on these bonds.

A. On which bonds do you mean?

Q. On bonds outstanding of the Reclamation District No. 2035. Isn't that a fact?

Mr. Acret: That is objected to as argumentative. The Birch Ranch and Oil Company doesn't pay on the bonds. They pay the assessment of the county treasurer and the amounts, when he makes them.

Mr. Crouter: I will revise the question to make it as counsel suggested.

The Court: Restate the question then. [127]

Q. (By Mr. Crouter): Please tell the Court whether it is correct that during a period of several years between 1933 and late in 1943 no payments of any calls or assessments whatever were made by the Petitioner corporation to Mr. Cole, the county treasurer, or to any other county treasurer, on account of reclamation bonds.

A. I can't understand why there wasn't some payments made between 1933 and 1943. While I wasn't here in 1933, didn't come here until 1937, I can't answer that question accurately.

Q. Let's take the period when you were there. In 1937, up until the end, near the end of 1943, please tell the Court whether it is a fact that no payment whatever was made on any call or assessments of reclamation bonds by the Petitioner to the county treasurer.

(Testimony of Robert R. Landrum.)

A. No calls were made by the county treasurer.

Q. And no payments?

A. No payments were made—well, I say no payments were made on these calls, because no calls were made. Things were in bad shap at that time. The county treasurer wasn't making the calls. He was looking after the interests of the landowners, the same as a lot of other districts were doing, so he didn't make the calls. He wasn't forced to, I guess, so he didn't. [128]

Q. Was there any request by the Petitioner which was the reason for not making any call or assessment?

A. Not to my knowledge.

Q. Is that all you know about why it was not made, that you can tell the Court?

A. That is all I know.

Mr. Crouter: That is all.

Mr. Acret: I have some questions now that are quite pertinent, that counsel opened up.

### Redirect Examination

By Mr. Acret:

Q. Do you know whether or not the Birch Ranch and Oil Company purchased interest coupons when they became due from other landholders?

A. In '37, you mean?

Q. Any time between '37 and '44.

A. Yes, they purchased some, I think.

Q. Do you know whether or not they purchased the interest coupons on the bonds that were owned



(Testimony of Robert R. Landrum.)

by the Hopkins, when and as they became due?

A. Yes, that is true. They did.

Q. Do you know whether at any time the Hopkins ever permitted any of the coupons to become past due without you being required to purchase them?

A. No, they would never let them go past due.

Q. Isn't it a fact that all the coupons of these 786 bonds owned by the Hopkins during that period were purchased by the Birch Ranch and Oil Company when and as they became due? A. Yes.

Q. And isn't it a fact that in the preceding case, which Judge Turner sat as judge, that the amount you paid for those coupons was allowed as a deduction by him in that proceeding?

Mr. Crouter: If your Honor please, I object to that.

Mr. Acret: I withdraw the question.

The Court: The record will show that.

Mr. Acret: Yes, the record will show that.

Q. (By Mr. Acret): Is the same true with respect to bonds that were owned by Lula M. Minter?

Mr. Crouter: I object to that, in that it is shown by Judge Turner's findings and conclusions.

The Court: That would be the best evidence.

Mr. Acret: That wasn't the point of that question.

Q. (By Mr. Acret): I am asking you, were there other coupons on bonds owned by other bondholders that the Birch Ranch and Oil Company purchased when and as they became due?

(Testimony of Robert R. Landrum.)

A. We purchased Miss Minter's coupons.

Q. That is the interest coupons?

A. Yes. [130]

Q. Those coupons you turned in to the county treasurer?      A. Yes.

Q. And under Section 348, which provides they may be turned in as money?      A. Yes.

Q. Do you know whether or not the Birch Ranch and Oil Company is the largest landowner in Yolo County, or one of the largest landowners?

A. Yes, they are, they were.

Q. Do you know whether or not it is one of the largest taxpayers in Yolo County?

A. I don't know about the taxpayers.

Mr. Crouter: I object to that, unless counsel makes it more specific. If he refers to state real estate taxes, I object, in that it is immaterial and irrelevant.

Mr. Acret: Your Honor, it only goes to account for these letters from Mr. Cole, which, naturally, would be to a corporation that is one of the largest taxpayers, one of cooperation, which a county officer would do in a little county of that kind, and explanatory of those letters.

The Court: I don't know that is material to this. I sustain the objection.

Mr. Acret: Very well, your Honor. That is all of this witness.

Mr. Crouter: Just a moment. That calls for some [131] cross-examination.

Mr. Acret: I was going to ask the Court—we

(Testimony of Robert R. Landrum.)

won't be able to finish tonight, and did your Honor intend to continue until a later hour?

The Court: It is five o'clock. I think it is about adjournment hour. I would like to finish this witness before adjourning, because my experience is, if you bring a witness back, you start all over again and cover the same grounds.

Mr. Crouter: I have just a few questions.

### Recross-Examination

By Mr. Crouter:

Q. Referring to your recent testimony here, did I understand you to say that certain interest coupons were purchased from a Miss Minter?

A. Yes.

Q. You mean, the Petitioner corporation purchased the coupons?

A. In some cases we would buy her coupons and turn them in as cash, when no call was made. She got her money that way.

Q. And, you say, turned them in. Do you mean they were turned over to the treasurer in lieu of cash?

A. Yes. We would buy them from her and when he would make a call, we would turn them in for payment.

Mr. Acret: May it be stipulated, counsel, for the benefit of the Court, that Section 3480 provides that a landowner may purchase interest coupons of the bonds of the district and turn them in as cash?

(Testimony of Robert R. Landrum.)

Mr. Crouter: On that matter, it is my understanding the Court will take judicial notice of the state laws, and it will be included in the brief, and I would rather handle it in that way.

Mr. Acret: It would be helpful to the Court at this time.

Mr. Crouter: I haven't examined that statute carefully.

The Court: The Court will take judicial notice, but if the briefs will set that out so the Court won't have to make an examination.

Mr. Acret: What is your Honor's situation with regard to California statute. It is helpful to have them printed.

The Court: Our library contains it.

Mr. Acret: I had it printed the last time for Judge Turner and also the entire Hopkins contracts.

The Court: I think that would be helpful if it were furnished in the brief or stated in the record, so the Court could have access to it, if counsel for Respondent is not in disagreement.

Mr. Crouter: I will be glad to check with Mr. Acret [133] on that.

Q. (By Mr. Crouter): Mr. Landrum, referring to your testimony that the Birch Ranch and Oil Company purchased other coupons of bondholders, apparently when they became due, please tell me who these other holders of the bonds were and what the totals were.



(Testimony of Robert R. Landrum.)

A. We stated that we purchased the Hopkins sisters' coupons and Miss Minter.

Q. Can you tell the Court about the amounts involved there?

A. Miss Minter's amounted to—she had ten bonds, so sixty dollars a bond every six months, that would be six hundred dollars, I guess—no, it wouldn't be six hundred dollars a year; three hundred dollars every six months.

Q. Were any of the Minter bonds—any bonds outstanding that were held by Miss Minter during the fiscal year 1944, or was this done prior to 1944?

A. Yes, they were outstanding in 1944.

Q. Referring to other holders, the Hopkins sisters, what amounts of coupons were purchased by the Petitioner from them?

A. Theirs was changing from time to time, so I couldn't tell you off hand. When I came with Mr. Birch in 1937, they had three hundred, I believe, twenty-three thousand or twenty-four thousand dollars worth of bonds. He was buying them back [134] from time to time, so I couldn't tell you what it was in 1944.

Q. If my memory is correct, I believe the stipulated facts show at any time there were three hundred ten thousand dollars of bonds which were acquired by Mr. Birch from the Hopkins sisters, and as I understand the stipulated facts and your testimony, also, bonds were held by trustees pending further payment to the Hopkins sisters.

A. There was a certain number of bonds held

(Testimony of Robert R. Landrum.)

in trust as security for fulfillment of that agreement that the Hopkins sisters had with Mr. Birch, which was to purchase these bonds that they owned.

Q. When coupons were purchased, did the Petitioner purchase merely the coupon or would it purchase a bond with the coupon?

A. No. In most cases, it was always the coupons only on what they owned; not what was in the trust.

Q. Were those purchased usually for the full face value of the coupons? A. Yes.

Q. As I recall, you stated that there were 786 bonds which were outstanding at one point, apparently prior to 1944, and those were all purchased by Birch Ranch and Oil Company, the Petitioner, purchased by Mr. Birch individually?

A. 786?

Q. Yes. [135]

A. Of the Hopkins—I don't believe that is true.

Mr. Acret: I just didn't put this witness on the stand as to the ownership of the bonds.

Q. (By Mr. Crouter): As I recall, he testified there were 786 bonds outstanding, as purchased by Mr. Birch or the Petitioner?

A. No, sir; I didn't testify to that.

Mr. Acret: We are getting into deep water here that he doesn't know anything about, and Mr. Birch will testify to.

Mr. Crouter: I believe that is all.

Mr. Acret: That is all.

The Court: What about a session for tomorrow? Will it be agreeable with counsel, being Saturday?

Mr. Acret: It would with one exception, your Honor. I need to make a living out of cases other than this. I have a client that is coming in at eleven o'clock——

The Court: You have a client coming in at eleven o'clock?

Mr. Acret: Yes, your Honor, that is my understanding, and I might not get that case if I were not there.

The Court: How much time will it take, so we can estimate the amount of time. Of course, Mr. Birch will have to testify, and I guess his examination will be fully as long as Mr. Landrum's.

Mr. Acret: About the same time. [136]

The Court: We have consumed about three hours on this.

Mr. Acret: A half an hour, I would say, for Mr. Birch's testimony, as far as our direct examination is concerned, and maybe less. Mr. Landrum's was taken up by putting in the documents, which takes a little longer. There are no further documents, no further documentary evidence, that I can recall at this time.

The Court: What is Respondent's counsel's estimate as to time?

Mr. Crouter: If your Honor please, it would chiefly depend on what the Petitioner offers. I would say double the time they estimate for their direct would cover it.

The Court: If that took a half an hour, you would have an hour and a half?

Mr. Crouter: No, the cross-examination would be about the same time as their direct, as far as Respondent's case is concerned. I am glad to state at this time that Respondent will have nothing except some documentary evidence, as far as I know.

Mr. Acret: Concerning all of which we can probably stipulate.

The Court: Well, the Court wants to know about this question of a session tomorrow. Saturday ordinarily is not a day Court is held, and, of course, the Court is anxious to [137] finish this case. We have a case set Monday.

Mr. Crouter: I could be here, if the Court please, although it would disturb some private arrangements, but I can be here if the Court says, if the Court sees fit. I might say that the case scheduled for hearing on Monday, the attorney for the Respondent has advised me it will probably be about a one day case. Beyond that, I don't believe there are any cases for hearing.

The Court: No, the case for Tuesday, I understand, is likely to be settled.

Mr. Crouter: That is a probable settlement.

The Court: In view of everything, I guess we had better let this case go for Monday.

Mr. Crouter: I wonder if we could have it Tuesday?

The Court: Would Tuesday morning suit you better, in view of the fact that stont parties are out of town?



Mr. Crouter: Yes, they are down in San Diego and Arizona.

The Court: I think this case might go to Tuesday morning at ten o'clock, if that is agreeable. We can probably save time. In the meantime, counsel can be thinking about the shortcuts that can be taken.

Mr. Acret: Or more testimony, one or the other.

The Court: This case will be resumed, the trial of it, on Tuesday morning at ten o'clock. The Court will take [138] a recess now until Monday morning at ten o'clock.

(Whereupon, at 5:10 o'clock p.m., an adjournment was taken until ten o'clock a.m., Tuesday, February 15, 1949.)

Filed T.C.U.S. March 8, 1949. [139]

[Title of Tax Court and Cause.]

(Met pursuant to adjournment.)

Before: Luther A. Johnson,  
Judge.

Appearances:

GEORGE ACRET,

1210 Quinby Building,  
650 S. Grand Avenue,  
Los Angeles, California,

Appearing for the Petitioner.

EARL C. CROUTER,

(Honorable Charles Oliphant,  
Chief Counsel, Bureau of  
Internal Revenue)

Appearing for the Respondent.

### PROCEEDINGS

The Court: I believe we were to resume this morning the case of Birch Ranch & Oil Company.

The Clerk: Docket Number 8720, Birch Ranch & Oil Company.

Mr. Crouter: In this proceeding, if the Court please, so long as we are talking about the pleadings, you will recall there were certain amendments of the Petitioner, amended petition, in the Birch case, and Respondent has prepared the usual written answer to such amended petition, and I ask

leave to file this at this time so our pleadings will be complete.

The Court: That completes the pleadings for both sides, I believe.

Mr. Crouter: I believe that is so.

The Court: I believe Petitioner was engaged in introducing testimony, was he not, when we recessed?

Mr. Acret: Yes, your Honor. We are ready to proceed.

The Court: Call your first witness.

Mr. Acret: Take the stand, Mr. Birch. I don't believe he has been sworn.

The Court: The oath was administered last week with the other witnesses.

Whereupon, [142]

#### A. OTIS BIRCH

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Acret:

Q. You are the A. Otis Birch that is named in the stipulation of partial facts herein?

A. I am.

Q. From the time of the formation of the Birch Securities Company, that was about October, 1934, wasn't it?

A. The dissolution took place then.

(Testimony of A. Otis Birch.)

Q. No, I say the formation of the company was about October, 1934. Is that correct?

A. Yes, October 15, 1935.

Q. And you became the president at that time?

A. Yes.

Q. And continued as such up to September 30, 1944?

A. Yes.

Q. And the company kept its books on the basis of the fiscal year ending September 30th?

A. Yes, that was the close of the fiscal year.

Mr. Acret: By the way, counsel, could we put in at this time the income tax return for 1942?

Mr. Crouter: If counsel desires it at this time, Respondent will be glad to offer as Respondent's Exhibit next in the case the Birch Ranch & Oil Company income and declared value excess profits tax return form 1120 for the fiscal year ending September 30, 1942, this return having been filed in the Sixth California collection district.

Mr. Acret: I would like to have it as an exhibit also of this Petitioner, your Honor.

The Court: You want it as a joint exhibit?

Mr. Acret: Joint number.

The Court: Is that agreeable?

Mr. Crouter: I don't see any necessity for that, if the Court please.

Mr. Acret: We would like to have it as a reference number as one of our exhibits.

Mr. Crouter: That is agreeable.

The Court: What will be the number of the exhibit?



(Testimony of A. Otis Birch.)

The Clerk: It will be 13F.

The Court: 13F. That is the income tax return of the Petitioner corporation for the fiscal year 1942. Is that correct?

Mr. Crouter: That is correct, and I believe I had better call to counsel's attention that there may be a tentative return involved there. I don't know whether counsel is familiar with this.

Mr. Acret: Whatever counsel has, we don't want anything but the facts. Counsel calls my attention to the fact there is also a tentative return attached to it. We have no objection to it.

The Court: Both documents, I assume, will constitute that exhibit.

Mr. Crouter: Yes, sir.

Mr. Acret: It bears Mr. Birch's signature.

The Court: And the parties will be granted leave to substitute photostatic copies.

(The document above referred to was received in evidence and marked Joint Exhibit 13F.)

Mr. Acret: Inadvertently, starting in this morning here, looking at some papers, I referred to the Birch Securities Company in asking Mr. Birch the questions I asked. I intended to say, "Birch Ranch & Oil Company."

Q. (By Mr. Acret): It was the Birch Ranch & Oil Company that was incorporated in October, 1934?      A. Yes.

Q. I meant to ask that. May it be understood

(Testimony of A. Otis Birch.)

that the question referred to the Birch Ranch & Oil Company?

You became president of the Birch Ranch & Oil Company at that time?      A. Yes.

Q. And remained such up to September 30, 1944?

A. I did.

Q. Do you know who owned the bonds of the Reclamation District during the year 1944, up to September 30, 1944?      A. Yes.

Q. Who did own those bonds?

Mr. Crouter: If your Honor please, I call for the record evidence on this. I believe that type of evidence should be reflected by writings, and I call for the best evidence on it.

Mr. Acret: Well, your Honor, that is not evidence——

The Court: I think that is a fact that can be shown, if the witness knows. I will overrule the objection.

The Witness: May I have the question?

(The question was read.)

The Court: If you know, you can testify, answer that. If you don't know, of course, say so.

The Witness: The Birch Securities Company owned 1,594,000 bonds and the Hopkins sisters owned par value of 310,000 bonds; Lula M. Minter owned 10 bonds, or ten thousand dollars.

The Court: A thousand each, par value?

The Witness: Par value of ten bonds, and the Birch Ranch & Oil Company owned 86,000 par value.

(Testimony of A. Otis Birch.)

Q. (By Mr. Acret): When did the Birch Ranch & Oil Company acquire those [146] eighty-six, and from whom?

A. It acquired them in 1940 from the Great Republic Life Insurance Company.

Q. Do you know how much they paid for those eighty-six bonds?

A. Sixty-five thousand dollars.

Q. That was less than the par value?

A. Yes.

Q. Was there ever any transaction other than that one, so far as you know, where those bonds were sold for less than par up to September 30, 1944?

A. No, there were none sold that I know of.

Mr. Acret: Your Honor and counsel, there is a stipulation with reference to the purchase by Mr. Birch of the ranch from the Hopkins, that is, the Hopkins' share of the ranch, and the Hopkins taking the purchase price in bonds at their face value, eighty-seven hundred eighty-six thousand. Then there is a contract concerning Mr. Birch's repurchase of those, and a stipulation that there was such a contract.

The Court: Repurchase of the bonds?

Mr. Acret: Repurchase of 786 bonds.

Q. (By Mr. Acret): By the way, Mr. Birch, you owned, before the incorporation of the Birch Ranch & Oil Company, we will say, just the day before October 13, 1934—do you know what the

(Testimony of A. Otis Birch.)

ownership [147] of those bonds was, of the reclamation district?      A. Yes.

Q. What was that ownership?

A. Mrs. Birch and I owned 1,594,000 and the Hopkins sisters 310,000; Lula Minter 10,000, and the Great Republic Life 86,000.

Q. Then, between 1925 and 1934, you purchased from the Hopkins the difference between 786 bonds and 310 bonds; is that right?

A. From the Hopkins?

Q. Yes.      A. Yes.

Q. What did you pay them for those bonds?

A. I paid them par value for them.

Q. As to whether or not you paid them interest, all accumulated interest on those bonds, up to October 15, 1934?

A. Yes, we paid them accumulated interest.

Q. Did you do the same as to the bonds, the remaining bonds owned by them, of the district?

A. Owned by Hopkins?

Q. Yes.      A. Yes.

Mr. Acret: In the case before Judge Turner, your Honor, we had the Hopkins' contracts in evidence. They are attached as an exhibit to the Petitioner's petition in that [148] case, Exhibits A and B. I offer those contracts in evidence herein by reference. I have the originals, but that is a printed petition; it is easy to read them, and I think that is the easiest and most effective way.

The Court: Without objection—

Mr. Crouter: If your Honor please, I would



(Testimony of A. Otis Birch.)

like to be heard on that. I don't believe that is a proper procedure, if your Honor please. I believe we should have, right in this record, and I would like to have for direct reference——

Mr. Acret: Well, I have them here. I offer the originals at this time, then.

The Court: What is it you offer?

Mr. Acret: The contract between A. Otis Birch and M. Estelle C. Birch.

Q. (By Mr. Acret): M. Estelle C. Birch is your wife? A. Yes.

Q. And was commencing along prior to 1920?

A. She was.

Q. And still is? A. Yes.

Mr. Crouter: What is the date of that?

Mr. Acret: Contract is dated January 10, 1925, and Louise Smith Hopkins.

Mr. Crouter: May I see the document? [149]

Mr. Acret: I will offer first the one dated January 1, 1924, Ruth Smith Hopkins.

The Court: Any objections?

Mr. Crouter: May I examine it just a moment, if your Honor please.

No objection.

The Court: That will be admitted then as Petitioner's Exhibit No.——

The Clerk: 14.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 14.)

(Testimony of A. Otis Birch.)

Q. (By Mr. Acret): Mr. Birch, I show you that just to refresh your recollection. You notice that is the 1924 one. Just notice the signatures at the end, and that will recall the contract to your recollection.

A. Yes, that is correct.

Q. Was a contract similar to that entered into with Louise Smith Hopkins?

A. It was identical.

Q. They were sisters? A. Yes.

The Court: The one offer was 1924 and now you are going to offer 1925? [150]

Mr. Acret: Yes, sir.

The Court: Same parties?

Mr. Acret: The one I am going to offer happens to be the other sister, I think.

The Court: There were two Hopkins sisters. One was named Ruth Hopkins and the other was Louise Smith Hopkins?

Mr. Acret: Yes.

Mr. Crouter: No objection.

The Court: The contracts between those parties mentioned, dated January 10, 1925, will be admitted as Petitioner's Exhibit No. 15. Is that correct?

The Clerk: Yes, sir. Exhibit No. 15.

(The document above referred to was received in evidence and marked Petitioner's Exhibit No. 15.)

Q. (By Mr. Acret): This one, Mr. Birch, is between you and Mrs. Birch and Louise Smith Hopkins. Was there an identical one entered into at

(Testimony of A. Otis Birch.)

the same time, with the other sister, Ruth Smith Hopkins?      A. There was.

The Court: And also in 1924, was it, both sisters?

Mr. Acret: They were entered into at the same time, were they, all these contracts?

The Witness: Yes, the first one you showed was in [151] 1924, and this one, I believe, is 1925.

The Court: And there was a contract with each of the two sisters at each of those dates; is that right?

The Witness: That is correct.

The Court: The contracts were identical?

The Witness: Yes, sir.

Q. (By Mr. Acret): I now notice this bears the statement on it, "Cancelled. Louise Smith Hopkins. March, 1944." Was that contract delivered to the Birch Securities Company at the same time?      A. It was.

Q. Do you know, was it at that time that the Birch Securities Company bought the 310 bonds you mentioned from the Hopkins?

A. They finished the buying as of that date.

Q. And paid what price?      A. Par value.

Q. Did you likewise receive a contract of Ruth Smith Hopkins, received it back, marked cancelled, in the same way and at the same time?

A. We received the contract back but it wasn't marked, "cancelled."

Q. But it was intended to be?

A. Yes. It was paid in full.

(Testimony of A. Otis Birch.)

Mr. Acret: Now, for the Court's convenience, I will [152] state that those contracts are printed and they will be much easier to read in the petition, in the first case, and they are attached as exhibits to the petition. Also, I offer, by reference, in evidence, portions of what I referred to as the California Reclamation Act.

The Court: That is the state law of California?

Mr. Acret: Yes, your Honor, 3480. It is printed at page 128 of the appendix, filed in support of the Petitioner's opening brief in the former proceeding.

The Court: Any objections?

Mr. Crouter: If your Honor please, as to that, I do just object on formal grounds, if your Honor please. I have no objection if the Court wishes to refer to it in that manner, and it is shown as a correct copy of the state statute, but we can easily refer to the state statutes and Respondent will include that in the brief.

The Court: In other words, it is not necessary to encumber the documentary evidence any more than necessary. If counsel can agree to the state law of California, if that is set forth in the brief, or some way, so the Court can have the benefit of it, I would appreciate it.

Mr. Acret: The act is rather lengthy; naturally with the——

The Court: I mean, just those portions deemed pertinent here could be set forth. [153]

Mr. Crouter: With respect to the offer, if the Court please, that statute is fairly long, and in our



(Testimony of A. Otis Birch.)

briefs I would attempt to include only the portions that bear on the issues here. I have noticed there are several small subsections of that Reclamation Act, which have been reviewed. I do not know whether what counsel offers was all outstanding and in effect during the years or not.

The Court: The Court would like very much if counsel could agree as to what the law was in effect at that time.

Mr. Crouter: I would be glad to do that and include it with our brief.

Mr. Acet: Counsel and I seem to be able to reach an agreement on matters of that kind. I am sure there won't be anything standing in the way of our doing so. I just wanted to avoid the necessity of reprinting that.

The Court: You called attention of that excerpt attached to your other——

Mr. Acet: Yes, commencing at page 128 of the appendix to petitioner's opening brief in the former proceeding. Also, I have set up some additional portions that are pertinent to this proceeding in the Memorandum of Points and Authorities that I have filed herein.

Mr. Crouter: I object to the latter, if the Court please. It is not a factual presentation at all; it is just [154] a legal argument.

The Court: Yes, that won't go in as part of the evidence.

Mr. Acet: Well, that hasn't anything to do with

(Testimony of A. Otis Birch.)

the evidence at all. I am stating it for your Honor's convenience.

The Court: I understand counsel has done that for the convenience of the Court.

Q. (By Mr. Acret): Mr. Birch, you mentioned that the Birch Ranch & Oil Company purchased the 86 bonds from the Republic Life in 1940. Do you know how they tended to do that?

A. I didn't buy them direct of the Great Republic Life Insurance Company. The Great Republic Life Insurance Company was taken over by the Postal Union Insurance Company, and the Postal Union Insurance Company began an action in the District against the owners of the bonds for the collection of those 86 bonds, particularly the past due interest that hadn't been paid. Therefore, in order to protect the land in the district, we contracted with the Postal Union Insurance Company for the purchase, by giving a mortgage on some property we had.

Mr. Acret: I don't want to be in the position of going back on the stipulation, your Honor, but on page 13, my recollection is, I made a little check mark after it here, the bottom paragraph, counsel and I left open the question of the [155] correctness of that statement. I questioned it and it was to be subject to further investigation. I would like to ask Mr. Birch with regard to it.

Q. (By Mr. Acret): Mr. Birch, in the stipulation it says, "Beginning with 1937, and until 1943, no amount has been paid in any year by the peti-

(Testimony of A. Otis Birch.)

tioner as interest on the \$1,594,000.00 of such bonds transferred by Birch and his wife to the Birch Securities Company.” Do you know whether or not that is correct?

A. Yes, I know, but it is not correct.

Q. In what respect is it not correct?

A. It seems to be the common expression that we pay interest into the county treasurer to pay the interest on the bonds, whereas the proper notation and entry would be that we pay the assessment that is levied by the district to meet the interest on the bonds.

Mr. Crouter: Before we leave that, if your Honor please, I object to that question and answer as not in accordance with the stipulated facts, and move they be stricken. Now, if the Court please, I believe the witness does make a distinction between the terminology to be applied to any payments, that is, whether they are interest or assessment or taxes upon the property. I am not too much concerned with terminology he may use, but I am concerned with the question [156] whether any amount was actually paid, any amount of money was paid to the county treasurer or to the Reclamation District. I take it, the effect of his testimony is that the payments were made.

Mr. Acret: He hasn't testified yet. I am coming to that. This is preliminary explanation.

The Court: The method of payment will be determined from the evidence, and as I understand,

(Testimony of A. Otis Birch.)

what the witness now is asked is with reference to the terminology of those expressions.

Mr. Acret: That is right, your Honor, and he is giving that preliminary explanation.

The Court: I understand counsel has no objection to that extent.

Q. (By Mr. Acret): That reminds me, Mr. Birch, you speak of the interest being paid on the Hopkins bonds. How was that done? What was the practice that was followed while you and Mrs. Birch owned the land of the district, that is, that part of the district comprising the ranch?

A. Well, for the first six years of the contract, beginning with 1925, the first payment was made to the Hopkins through their collection from the county treasurer of Yolo on the coupons that matured on the bonds. Then Mrs. Birch and I paid them \$78,600.00 annually as the redetermination or purchase of 6,600 par value of bonds.

Q. Well, how was the interest paid on the bonds? What was the procedure in this first six years?

A. Mrs. Birch and I paid the assessment, based on the call from the county treasurer, on the bonds, to provide for the interest payment, and the Hopkins cashed their coupons.

Q. You say that is the first six years. That would take it up to 1931. What was the practice followed by you and Mrs. Birch from 1931 to 1934?

A. We purchased the coupons from the Hopkins by paying them face value of the coupons as they matured.



(Testimony of A. Otis Birch.)

Q. The interest coupons, that is? A. Yes.

Q. What did you do with those coupons? Were they turned in to the county treasurer?

A. We deposited them with them.

Q. For what purpose?

A. To cash them when there would be money available.

Q. I mean, keeping in mind the provisions of the statute, for what purpose were they turned in, the same as money? A. Yes.

Q. Showing you Petitioner's Exhibit No. 10, is that the usual form of receipt received from the county treasurer on payment of either turning in coupons or turning in money? A. Yes. [158]

Q. That is referring to the second page of Exhibit 10, the first page being a check; is that correct?

A. Yes.

Q. Between 1925 and 1934—I believe it is in the stipulation that the deductions were made by Mr. and Mrs. Birch—did you make the deductions of the amounts paid to the county treasurer to meet interest on the bonds?

A. We did, always.

Q. When you and Mrs. Birch received back from the county treasurer such interest, did you take account for it as part of your income?

A. We did not.

Q. Why not?

A. Because it was tax exempt income.

Q. Do you know how many times that proce-

(Testimony of A. Otis Birch.)

dure, between 1925 and 1934, was questioned by the Commissioner?      A. Every year.

Q. Was that procedure ever disapproved during that period by the Commissioner?

A. No, not once.

Q. Was there any intention on your part in forming the Birch Ranch & Oil Company to in any way avoid taxes?      A. None whatever.

Q. Forming the two corporations, the Birch Ranch & Oil Company and the Birch Securities Company, was that to [159] enable you to be able, on the one hand, to deduct the amounts paid to the county treasurer to cover the interest on the bonds, and, on the other hand, to receive the interest from them without having it part of the income?

A. No, no more than when we owned the bonds personally, individually.

Q. Now, taking the next sentence on page 13 of the stipulation, referring to the Birch Securities Company, it says: "Nor has it paid any amount as interest on the \$86,000.00 of such bonds held by the Great Republic Life Insurance Company." That seems to refer not only to April, 1936, until April, 1943, but to all times, the way the stipulation is worded. What is the fact as to the payment of any assessments to meet interest?

A. My recollection is that assessment was paid in 1937, but subsequent to that, up until 1943, there were no payments.

Q. Why were there no payments?

A. Because we weren't able to raise any funds

(Testimony of A. Otis Birch.)

through our applications for loans through the Reconstruction Finance Corporation, and the various banks in the country.

Q. Well, is the answer, because you were unable to make the payment, didn't have the money?

A. Didn't have the money and couldn't borrow any.

The Court: Was the depression period still on at this time? Did that have anything to do with your condition? [160]

The Witness: Yes, that was.

The Court: The depression which began in '29?

The Witness: Yes, but we didn't feel the pinch until about '31 or 2.

Mr. Acret: The depression really hit out on the coast about the middle of 1933. It drifted out here as a wave. Our bank blew up in March, 1933, is my recollection.

The Witness: I might add that the bank that we had our account at in Sacramento failed and tied up our funds there, besides we owed them——

The Court: When did that occur?

The Witness: That was in 1931 or 2.

Mr. Acret: I guess the record shows all assessments were paid on the bonds, all assessments of the Reclamation District were paid during the fiscal year ending September 30, 1944.

Q. (By Mr. Acret): They were paid right up to date, weren't they, all the assessments of the district?

Mr. Crouter: If your Honor please, I have no

(Testimony of A. Otis Birch.)

objection to that insofar as it calls for the payment of money, but I do object to any conclusions as to whether it was an assessment, and so forth. I believe what counsel seeks is really shown by the record.

The Court: Isn't that contained in the stipulation? [161]

Mr. Crouter: No, that is not covered by the stipulation, but I think everything counsel seeks to establish is covered by record evidence, such as the checks.

The Court: Of course, if it is already in evidence, it wouldn't be necessary.

Mr. Acret: What bothers me a little bit is the way counsel drew up the stipulation. He calls it all the way through "payments of interest," and that is only a matter of nomenclature, and the evidence would show what the facts were.

The Court: You want to offer evidence to sustain your contention that it was not interest?

Mr. Acret: In other words, it is whatever it is by reason of the law.

Mr. Crouter: That is part of the basis of my objection, if the Court please. It does call for a conclusion and we will probably be arguing about that until our last brief is filed.

The Court: The witness can't establish a conclusion of law. He can state the facts as he understands them.

Mr. Acret: Nevertheless, I have to embody in



(Testimony of A. Otis Birch.)

my question and frame the question properly as I understand to be the effect of the law.

May I have the question read?

(The question was read.)

Mr. Crouter: I object further; leading and [162] suggestive and improper direct examination.

Mr. Acret: I withdraw the question.

Q. (By Mr. Acret): Mr. Birch, do you know whether or not there were any payments that were due the district to meet interest on the bonds accruing during the fiscal year ending September 30, 1944, that were unpaid?

A. I can't recall that there were any that were not paid.

Q. In other words, by 1944 your companies were in a little different financial shape, and able to take care of the various obligations?

A. Yes. We had sold some properties that provided some cash, and we were able to make some loans then, and had liquidated some of the other indebtedness to various creditors, something over a million dollars.

Q. That reminds me, Mr. Birch, one other matter that was left open in the stipulation, your Honor, and I want counsel to understand I don't want to be in the position in any way of going back on the stipulation, but I think this was left open also.

I call your attention to this paragraph on page 12 of the stipulation, Mr. Birch. I direct your attention to it, and read as follows: "On October 15,

(Testimony of A. Otis Birch.)

1934, Birch and his wife organized Birch Ranch & Oil Company, the Petitioner herein, [163] and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership of which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000.00."

This property you kept out, property having a value of about \$600,000.00, did you have any purpose in keeping that out and not transferring it to the corporations?           A. Yes.

Q. What was that purpose?

A. That was to protect the other creditors.

Q. Your personal creditors?           A. Yes.

Q. That is so you and Mrs. Birch would still have some personal assets?           A. Yes.

Q. Passing on to this next page——

The Court: You are referring now to an extract you are going to read from the stipulation of facts?

Mr. Acet: Yes, your Honor.

The Court: I think it might be well to indicate when you begin and when you end, when you are reading.

Mr. Acet: Very well, your Honor.

Q. (By Mr. Acet): That property that you held out, was that ever any—was any part of that ever transferred to the Birch Ranch & Oil Company or the Birch Securities Company or the Birch Holding Company?

(Testimony of A. Otis Birch.)

The Court: That is the \$600,000.00?

Mr. Acret: Yes, sir.

Q. (By Mr. Acret): The \$600,000.00 property, was any of that transferred to these corporations?

A. No.

Q. What is it? A. I believe not.

Q. Now, Mr. Birch, in the stipulation on page 14, it reads as follows: "On its books for the fiscal years 1937 and 1939, the taxable years herein, the Petitioner accrued \$120,000.00 to represent some on the entire \$2,000,000.00 par value of issued bonds of Reclamation District No. 2035." Is that a correct statement. Is that statement strictly correct, to represent interest? A. No.

Mr. Crouter: I must object to this on the same grounds, that this is a matter for the Court's determination, under our Revenue Act, and under the state law.

The Court: Counsel is asking the witness what he understood the payment was for. [165]

Q. (By Mr. Acret): What was your understanding that was for, this accrued \$120,000.00?

A. Well, the interest of \$120,000.00 accrued on the bonds and assessment was levied on the land to provide for the same amount of money by issuing a call by the treasurer of Yolo County.

Q. Was the \$120,000.00 accrued to meet that expected call?

A. The interest had accrued and they made the call through the district.

(Testimony of A. Otis Birch.)

Q. I say, was the amount of \$120,000.00 accrued on the books to meet that call?

A. Yes, it was on an accrued basis.

Q. Now, it says here, on page 14——

The Court: Is it the stipulation you are reading now?

Mr. Acret: Yes, your Honor.

Q. (By Mr. Acret): “For the fiscal year 1937,” and I want you to listen to this, Mr. Birch, “it entered the \$18,600.00 paid to the Hopkins sisters, as above stated, as a loan to the Birch Securities Company.”

Do you know how that happened to be put on the books that way? [166]

Mr. Crouter: If your Honor please, I think I will have to object to that. I thought we had reduced these things to final form. If we are going into the books and records, I call for the best evidence, and this is a little bit afield from our main point. I did not know counsel wished to go into these matters. I call for the best evidence, the books and records, and so forth, so we can see exactly what the documents are. I object to establishing those things by oral testimony or trying to.

Mr. Acret: Your Honor, we have stipulated the best evidence. That is the facts. They accrued those on the books in that manner, and I want to show it is a mistake, who made the mistake, and what was done with it.

The Court: In other words, you want to show the book entry was in error?



(Testimony of A. Otis Birch.)

Mr. Acret: The accountant made the error.

The Court: The stipulation contains the fact that the book entry was so and so, and you want to show it, as I understand it, that it was an erroneous entry.

Mr. Acret: That is right.

The Court: If there is any controversy about the existence of that matter, or just a mere proof of what it was——

Mr. Crouter: I have no objection to a mere explanation by the witness of the stipulated facts. I thought counsel was seeking to establish something else. [167]

The Court: No, he is simply trying to stipulate what his understanding was.

Mr. Acret: I won't seek to establish anything different from the stipulation, except in the places counsel and I reserved, and this is in one of them.

Q. (By Mr. Acret): Do you know how that came to be entered in the books that way for 1937?

A. Yes.

Q. What was it?

A. We had employed a bookkeeper to open up the corporation books, and he interpreted that payment as a payment of interest, rather than a payment of assessment, and he treated the payment to the Hopkins as paying them interest on our obligations under the contract, rather than paying the assessment so that the Hopkins could cash the coupons that matured at that time.

Q. When did you first discover that was entered that way?

(Testimony of A. Otis Birch.)

A. When the question was raised by a field agent of the Federal government.

Q. What was done about it in subsequent years, with respect to the amounts paid to the district to meet interest on the bonds? Were they entered in that manner or in a different manner? [168]

Mr. Crouter: If your Honor, please, I object to evidence of this character. That certainly should be shown by some books and records. It has been apparent in this case, up to now, we have no original books or records reflecting any of these payments.

The Court: Any controversy about that?

Mr. Acet: If there is any controversy about that, I don't know—counsel had it before.

Mr. Crouter: I call for the best evidence, if the Court please. We are working in the dark, talking about books and records, and trying to establish it by oral testimony.

Mr. Acet: As a matter of fact, I don't think it makes any difference.

Mr. Crouter: Then I object, because it is immaterial.

Mr. Acet: Don't interrupt me, please, counsel.

Mr. Crouter: I am forced to.

Mr. Acet: Let me finish before you are forced to. As a matter of fact, I don't think it makes any difference, your Honor, because in the income tax returns for the year in question, the item is deducted as taxes paid, and that, coupled with the deficiency assessment, gives all the facts and leaves

(Testimony of A. Otis Birch.)

it, as a matter of fact, to just the legal conclusions to be derived therefrom. It is the same situation all over again. I don't think there is any matter of accounting involved here. I don't think there is any fact in this case, [169] your Honor, and counsel, that is or should be in dispute. It is simply a matter of legal question, of interpreting the Reclamation Act.

Mr. Crouter: What Mr. Acret recently said is part of the basis for my objection, if the Court please. His question appeared to me to be going into what is shown by books and records as separate and apart from what is shown by tax returns, and so forth. It seems to me the facts which would be necessary for the Court's determination of what those payments may have constituted are already in the record. My objection was chiefly to going into books and records and saying how they were shown and charged and listed.

The Court: Since the testimony of the witness, the point at which the books were entered to show payments of entry only and having been understood between counsel that was a matter that could be stipulated or explained by oral testimony, as to how that occurred, and then counsel followed that in his explanation to show that error did not occur again, I think that is all right. I don't think it calls for the necessity of books, if the witness knows that did not so occur again in the books.

Mr. Acret: That is the only thing that brought the subject up at all, was that correction.

(Testimony of A. Otis Birch.)

Q. (By Mr. Acet): Mr. Birch, in participating as one of the landowners [170] in the formation of Reclamation District No. 2035, did you or your associates have any intention of tax avoidance?

A. No, it never occurred to us.

Q. And you and your wife and Mr. and Mrs. Conaway spent in performing the contract for the improvement of the district, as stated in the stipulation, an amount equal to or in excess of two million dollars?

A. Yes.

Q. For which you received the warrant that is in evidence or that is referred to in the stipulation, the two million dollar warrant?

A. That is correct.

Q. As stated in the stipulation, an election was held to promote a bond issue against the district to pay the warrant?

A. Yes.

Q. As one of the landowners, did you participate in the proceedings for it, in the election for the bond issuance?

A. I didn't quite get that.

Q. Did you, as one of the landowners in the reclamation district, participate in the election relating to the bond issuance?

A. We did.

Q. Did you in any way have any intention of tax avoidance in connection with that matter?

A. None whatever. [171]

Q. How long was it that you waited for your money for the work that you and Mr. Conaway did in improving the district from the time of the commencement of the work until the time that you got the money or the bonds in payment therefor?



(Testimony of A. Otis Birch.)

A. About six or seven years.

Q. During that time, as the work was performed, did you make any effort to get warrants to pay you up to date?

A. No. That was the common practice in other districts, but the Birch Oil Company, as a contractor, might have presented statements monthly for the work performed, and the district, in that event, would issue you a warrant, representing the amount involved. The contractor then, as the ordinary common practice, would present that warrant to the county treasurer to cash it. If there were no funds on hand to cover it, he would stamp it, "No funds available," and from that day on it would draw seven per cent. If we had done that monthly for the first six or seven years, we would have accumulated several thousand dollars more earning. Then there would have been a greater bond issue to cover the entire expense.

Q. As a matter of fact, the state engineers estimate was some two million two hundred odd thousands, was it not, for the construction costs in the district?      A. Yes.

Q. And you only took the one two million dollar warrant?

A. That is right, after the work was completed.

Q. You didn't avail yourselves of the seven per cent interest?      A. Not at all.

Q. Which would have an additional basis of tax deduction?

(Testimony of A. Otis Birch.)

Mr. Crouter: I object to that, on the ground it calls for a conclusion.

Mr. Acret: That is argumentative.

The Court: Argumentative.

Mr. Acret: Lawyers sometimes like to put a point over. Sometimes it is irresistible. I think that indicates I have just about covered the subject.

The Court: I think so. Let's take a ten minute recess.

(Short recess taken.)

The Court: The witness will resume the stand.

Mr. Acret: Counsel may cross-examine.

### Cross-Examination

By Mr. Crouter:

Q. Referring to your testimony, Mr. Birch, about who owned the bonds of the reclamation district, we have been talking about, during the fiscal year 1944, is there any written record that you have available here so that you can show the Court exactly who the owners were with respect to any bonds during the fiscal year 1944?

A. No, I haven't any memorandums. [173]

Q. Is there any stock record book or certificate book of any reclamation district, that you have here in the court room?

Mr. Acret: Just a moment. Your Honor, counsel overlooks the fact that Reclamation District is a state agency, the offices of which are up in northern California. How would we be expected

(Testimony of A. Otis Birch.)

to have any records of the reclamation district?

Mr. Crouter: I am asking Mr. Birch.

The Court: Counsel asked him if he had it and he said he didn't, as I understand it.

Q. (By Mr. Crouter): Mr. Birch, please tell the Court from the very inception of any Reclamation District 2035, about 1925, what, if any, official position you held in the reclamation district. Just tell the Court year by year as to that, as that went along, what, if any, officer you were of the reclamation district, clear down through the year 1944.

A. You mean, when it was organized, back in 1919 to 1944?

Q. Whenever it was first organized.

A. It was organized in 1919. The petition was made in 1918.

Q. Well, the reclamation district, as such, did not really start until 1925?

A. No, sir. That was the date the bonds were issued, [174] after the work had been performed.

Q. Were you an officer of any Reclamation District 2035 between 1925 and the end of 1944?

A. I believe not.

Q. You never were?

A. No. I might have been in the early part, but not to my recollection after the bonds were issued.

Q. You were never a trustee of the district at any time?

A. I was, I say, for a time, but my recollection

(Testimony of A. Otis Birch.)

is not after the bonds were issued. I wasn't one of the trustees on its organization.

Mr. Acret: Did he say he was not?

The Witness: I was not. The supervisors appoint the trustees, and I wasn't one of them.

Q. (By Mr. Crouter): Well, now, Mr. Birch, there is in evidence in this case, Exhibit 8——

Mr. Acret: May it be understood the supervisors to whom he refers, so it won't have to be picked up on further examination.

The Court: Who are the supervisors, the directors of the district?

The Witness: The county supervisors appoint the trustees of the district.

The Court: All right. [175]

Q. (By Mr. Crouter): Did you ever have anything to do with the election or designation of any trustee?

A. I might have suggested my father-in-law to be a trustee.

Q. That was Mr. Conaway? A. Yes.

Q. You suggested Mr. Armfield, also, your lawyer, did you not? A. Not I, personally.

Q. You never did?

A. No, I didn't personally. Mr. Conaway was up there.

Mr. Acret: I object to counsel saying "his lawyer, personally." Mr. Armfield was lawyer for the reclamation district, a lawyer, and a local banker up there.



(Testimony of A. Otis Birch.)

Mr. Crouter: He answered the question.

Q. (By Mr. Crouter): I proceed with the matter I started on a moment ago, and show you Exhibit 8 in evidence. This seems to be a cancelled original or sample of bond number 2,000 for \$1,000.00 and a notation on the margin reads "Cancelled on exchange for refunding bond number R-2,000, Roy E. Cole, treasurer, Yolo County."

Now, this seems to be the last of a first series of bonds, is that correct, number 2,000. Is that the way it [176] operated?

A. Yes, to the best of my knowledge, there were two thousand bonds, and it was numbered 2,000. It must be the last one.

Q. You will notice that this carries a date of 1925 in here, January 1, 1925, being on the very last line, apparently being an issuance date.

A. If that is the issuance date, that is correct.

Q. Now, the thing I'm getting to, Mr. Birch, do you have here in the court room any original or exact copy of any reissued bond that you could show the Court and show me, so I can see how it reads?

Mr. Acret: Just a moment. That is objected to as immaterial. We have the certified copy of the record of the Superior Court, validating the first bond issue and validating the second bond issue, each of which contains a certified copy of the bonds of issue. It is objected to. To go into this is encumbering the record.

The Court: The record already contains the exact copies, as I understand. Is that right?

(Testimony of A. Otis Birch.)

Mr. Crouter: I disagree with that, if the Court please. The record shows certain proceedings way back in 1935, and they relate to what may have been authorized to be done, but they do not show by any court order entered in 1935 what was done as of a later date, and particularly whether any bonds [177] were issued and outstanding during the fiscal year 1944.

The Court: Were there any bonds issued subsequent to 1935?

Mr. Crouter: I would like to know from the witness.

The Court: Were there?

The Witness: Yes, the bonds were twenty-year bonds, a serial commencing maturity ten per cent in 1935. At that time we held another election for authorization of refunding bonds, and it was completed and those bonds were issued and they ran until 1945. Preceding that, about two years, we had given an option for the sale of the bonds and the ranch, and the option holders carried on the refunding again, and, of course, both of those first two refunding bonds were surrendered to the county for the last refunding bonds, which were dated 1945.

The Court: What particular bonds were referred to in the validating order of the Court?

Mr. Acret: Both proceedings, your Honor, the proceeding validating the first series of bonds, and then there was a proceeding validating the second series.

(Testimony of A. Otis Birch.)

The Court: By "second," you mean the refunding bonds?

Mr. Acret: Refunding bonds, and Mr. Landrum testified that the old bonds were turned in and the refunding bonds were issued in place of them, and the Birch Securities Company [178] received its share, that one million five hundred ninety-four thousand dollars.

The Court: Does it show bonds that were issued in lieu of these original bonds? Does the record contain any record of those bonds?

Mr. Acret: Mr. Landrum testified he received the bonds referred to in that record of the Superior Court. I don't know what the exhibit number is, but the copy of the bond is set up and Mr. Landrum identified it.

Mr. Crouter: If your Honor please, I merely want to pick up the story from Mr. Landrum. Your Honor will recall I asked Mr. Landrum certain questions, and I got the response, "Mr. Birch knows all about that and he will testify to it."

Mr. Acret: I wish counsel would be accurate and quote my words. I didn't say "Mr. Birch knows all about anything," because he doesn't, and neither do I, and neither does counsel. I said I didn't put Mr. Landrum on to testify as to the ownership of the bonds, but that I would put Mr. Birch on.

The Court: As I understand, Mr. Birch was to know all about the ownership of the bonds.

Mr. Acret: And he so testified.

(Testimony of A. Otis Birch.)

The Court: I don't know what the line of questioning counsel now is seeking, but we will go ahead and see what it is. I don't want to go back. In other words, this case has [179] already assumed pretty wide proportions, having been tried before two other judges. So, I don't want to go back over any beaten path and introduce any evidence already contained in the stipulation of facts or exhibits that have been offered. What was the question now?

Q. (By Mr. Crouter): I would like to ask, if the Court please, and I ask Mr. Birch, what, if any, written evidence do you have of any reissued bonds that were issued after or in connection with the reissuance indicated by Exhibit 8. In other words, do you have any copy of any bonds that were outstanding, so I can see the exact provision?

The Court: You mean, in Court now?

Mr. Crouter: Yes, anything that was outstanding during 1944.

The Witness: I haven't anything. All of the bonds representing any one issue would be on deposit with the county treasurer of Yolo County.

Q. (By Mr. Crouter): Referring to your testimony that an option was given to purchase, did you say the lands and the outstanding bonds?

A. Yes, sir.

Q. What was the date of that option?

A. About '43, in March, I believe. [180]

Q. Do you have a copy of any documents relating to that matter? A. Not with me, no.

Q. Was that an option to some other corpora-



(Testimony of A. Otis Birch.)

tion or person besides you and Birch Ranch & Oil Company?

A. Oh, yes, it ran to Mr. Rasmussen, and he sold it eventually to other individuals, who incorporated when they purchased it.

Q. Was he connected with Woodland Farms, Incorporated?

A. I believe so, and also the Con Ranch was another one.

Q. That date was March, 1943?

A. That was 1943. My recollection is that it was either February or March of 1943.

Q. I take it that was a written document of some kind?

A. Yes.

Q. Written option?

A. Yes.

Q. And a written agreement?

A. Yes.

Q. Was Birch Ranch & Oil a party to the agreement?

A. In selling the ranch and the land, yes, as a personal property.

Q. Were you and Mrs. Birch parties to the agreement in selling bonds?

A. Yes. [181]

Q. You don't have a copy of any of those documents relating to the transaction with Mr. Rasmussen or Woodland Farms, Inc.

A. I haven't it with me.

Q. Please tell the Court what, if anything, was done with the bonds that were outstanding and held by you and Mrs. Birch at the time, in March, 1943, when that agreement was entered into.

Mr. Acet: That is objected to as not in ac-

(Testimony of A. Otis Birch.)

cordance with the evidence. He didn't say "agreement." He said "option."

Q. (By Mr. Crouter): When the option was entered into?

A. What is the question now? What became of the bonds?

Mr. Acret: Objection. Also, if your Honor please, the question is assuming something not in evidence. The bonds owned by Mr. and Mrs. Birch, the testimony is that the bonds are not owned by Mr. and Mrs. Birch. They were otherwise owned at that time, and I presume this is speaking for the fiscal year ending 1944, up to the fiscal year ending 1944.

The Court: What fiscal year does he have reference to, any particular fiscal year? The Court inquires of counsel.

Mr. Crouter: I will withdraw the pending question and start further back, if the Court please.

Q. (By Mr. Crouter): You mentioned the Birch Securities Company, and I will ask you whether it is not a fact that the Birch Securities Company was suspended from doing business in California sometime in 1938?

A. Yes.

Q. How long did it stay suspended, according to your own knowledge?

A. Until it was disincorporated.

Q. When was that?

Mr. Acret: That is objected to as immaterial, unless it was before September 30, 1944.

Mr. Crouter: If your Honor please, I would like——

(Testimony of A. Otis Birch.)

The Court: I will overrule the objection. We will see what he is getting to. Answer the question.

Q. (By Mr. Crouter): The question is when it was disincorporated or when it was dissolved?

A. I don't know what the——

Q. Do you know when, if at any time, the Birch Securities Company was dissolved?

A. It completed dissolution in October of 1944.

Q. Did it ever do business at all between 1938 and 1944, that is, Birch Securities Company?

A. I wouldn't say that it did any business. [183]

Q. Do I understand your testimony from the prior occasion here to be that during some portion of the time, before the end of 1944 or the end of the fiscal year 1944, the Birch Securities Company held the stock of the Birch Ranch & Oil Company. That is the way it was held for a long time, isn't it?

A. No. The Birch Securities Company never did hold the stock of the Birch Ranch & Oil Company.

Q. Then, it was the Birch Holding Company that held the stock directly? A. Yes.

Q. Then you and Mrs. Birch owned all the stock of the Birch Holding Company?

A. That is correct.

Q. Now, did the Birch Securities Company, during any of the years between 1938 and 1944, have issued to it, or did it actually hold any of these reclamation bonds? A. Yes.

Q. Which way were they handled? Were they bearer bonds?

(Testimony of A. Otis Birch.)

Mr. Acret: What?

Mr. Crouter: Bearer bonds, issued to bearer without the name of the holder.

The Witness: They didn't read "bearer" but they were negotiable. [184]

Q. (By Mr. Crouter): Tell the Court how any bonds were held by the Birch Securities Company during that period I have indicated and what amount of bonds, if you know.

A. The time they were incorporated in 1934, Birch Securities Company received \$1,594,000.00 in bonds.

Q. How long did the Birch Securities Company hold those bonds, if you know?

A. Until it was dissolved.

Q. What happened then with the bonds, in October, 1944?

Mr. Acret: Your Honor, I object to that as being immaterial. We will open up a field here that is outside and beyond the fiscal year that is in question here, and we ought to keep to the issues.

Mr. Crouter: Yes, I withdraw that. I was thinking of the calendar year there for a moment.

Q. (By Mr. Crouter): Please tell the Court whether it is a fact that during all of the fiscal year 1944 the Birch Securities Company was suspended from doing any business, by Court order, directed not to do any business under order of the Court?

Mr. Acret: Just a moment, please. That is objected to as assuming something not in evidence and not in accordance with law. Under the law of



(Testimony of A. Otis Birch.)

California, no company suspended by Court order purports to be suspended on request of the [185] Franchise Tax Commissioner by the Secretary of State.

The Court: Well, the witness can state what facts he knows. The legal effect of what the order is, probably the witness wouldn't be familiar to testify. He might not be qualified to know what the effect might be.

Mr. Crouter: I withdraw the question.

Q. (By Mr. Crouter): What, if any, investigation was pending during the fiscal year 1944, involving Birch Securities Company?

A. The state was attempting to collect about nine thousand dollars.

Q. Was it on that account that there were certain legal proceedings involving the question of doing business by Birch Securities Company?

A. No, not out of that, but from the fact the Birch Securities Company previously received the interest on the coupons that it held, and it treated that as an income.

Q. Do I understand that the State of California was seeking to impose some tax on Birch Securities Company?      A. Yes.

Q. And then the Birch Securities Company just ceased to have any transactions of that kind, pending a clarification of that in the Courts. Was that the situation?

A. I don't know that was the result. We didn't

(Testimony of A. Otis Birch.)

have the money to pay any taxes; therefore, they haven't anything to [186] collect.

Q. Do you have any books or records here of Birch Ranch & Oil Company reflecting any account relating to payment of money to the county treasurer with respect to reclamation bonds?

A. No, I haven't any books.

Q. Were there any such books or records kept?

Mr. Acret: That is objected to as cumulative, your Honor. We have the original evidence here, and that is the return, certified checks, with the county treasurer's receipt for all the payments that are material to this proceeding, to wit, all the payments made to the Reclamation District during the fiscal year ending 1944, and you couldn't ask for more than that. There is the checks totaling \$221,000.00. Why go outside of those?

Mr. Crouter: I submit, if the Court please, it is a proper question, and I would like to have it answered.

The Court: The reporter will read the question.

(The question was read.)

The Court: Answer the question. Were there any such books kept?

The Witness: I didn't keep any book personally for the bonds I owned, when I owned them. There was some entry in the books of when the Birch Securities Company was organized, and also when the Birch Ranch & Oil Company bought those 86 bonds from the Postal Union. It made an entry

(Testimony of A. Otis Birch.)

of the ownership [187] of the ownership bonds.

Q. (By Mr. Crouter): Mr. Birch, my question is whether Birch Ranch & Oil Company, a corporation, kept any permanent records or books reflecting any payments of money to the county treasurer during the fiscal year 1944, such as the amounts shown by the exhibits 9, 10, 11 and 12 in evidence and before you?

A. Yes, our bookkeeper would make those entries on the Birch Ranch & Oil Company books.

Q. Where was the office of the Birch Ranch & Oil Company, if it had any, during the fiscal year 1944?

A. In the Auditorium Building, on the fifth floor.

Q. Where was it located?

A. Auditorium Building, on the fifth floor, Los Angeles, Fifth and Olive Streets.

Q. Does it still have an office there?

A. Yes.

Q. Are those records still kept? A. Yes.

Q. And that is approximately a mile from the Federal Building, where we are holding this hearing, isn't it? A. What?

Mr. Acet: If counsel wants those books and there is the slightest question about it, we will have them here, but it is purely cumulative. We have the original payments and [188] receipts. If your Honor feels that it is in any way clarifying, we will have them here, and chances are, I would say, probably in fifteen minutes. That is how easy it is.

The Court: There is an offer made to produce

(Testimony of A. Otis Birch.)

the books, as I understand it, by Petitioner's counsel.

Mr. Acret: It is objected to, however, as being cumulative and unnecessary. The best evidence is already in on those payments.

Mr. Crouter: This bears upon another matter I will refer to.

Q. (By Mr. Crouter): The office, then, is about a mile from the Federal Building. Is that correct?

A. Not more than a mile.

Q. Now, Mr. Birch, have you kept any permanent record of your own with respect to any of the amounts received by you and Mrs. Birch from the county treasurer, which was regarded by you, as I recall your testimony, as tax exempt?

A. I never kept any books personally.

Q. Do you have any complete record of that?

A. Only my checkbooks, bankbooks, evidencing the deposits.

Q. Showing deposits of such money?

A. Yes.

Q. Referring to your testimony about the length of time [189] that the payments were made to the Reclamation District, there was a period of several years when they were not made, and I believe you stated that was because of the depression years, and not having money available?

A. That is correct.

Q. Was that the only reason?                      A. Yes.

Q. Now, during those years, when those payments were made by the Birch Ranch & Oil Com-



(Testimony of A. Otis Birch.)

pany to the county treasurer, did I understand you to say that any persons, including yourself, who owned bonds, still collected this tax exempt interest from the county treasurer?

A. No, they didn't collect it from the county treasurer.

Q. So that if the record——

A. ——they collected—their interest would be that we would buy the coupons from the bondholders.

Q. By "we" do you mean you, individually, or the corporation, Birch Ranch & Oil?

Mr. Acet: That is objected to as not clear as to which year is being talked about.

Q. (By Mr. Crouter): Please tell counsel which year you are talking about and who do you mean by "we."

Mr. Acet: I asked counsel to tell the witness which year he is talking about. [190]

The Court: I don't remember just what the question was. What year did you understand you were testifying about?

The Witness: I understood I was testifying during the period which the assessments were not paid in to the county treasurer.

Q. (By Mr. Crouter): And that was roughly from sometime in 1937 down to the latter part of the calendar year 1943, was it not? A. Yes.

Q. During that period, the coupons were purchased by whom?

A. Either the Birch Ranch & Oil Company or

(Testimony of A. Otis Birch.)

personally by the individuals. The Birch Ranch & Oil Company, after 1934, guaranteed the contract with the Hopkins, and when the Hopkins were assisting on either the payments or six months extension through this guarantee of the Birch Ranch & Oil Company, and to satisfy them, for them to consent to an extension of a six months period at a time, we would purchase the coupons from them and pay them face value for them, \$30.00 a coupon.

Q. You say there was a guarantee. Was that in writing? A. Yes.

Q. Do you have a copy of that available, or original?

A. I believe that is included in the Hopkins extension agreement. [191]

Q. One of the documents offered this morning?

A. Well, I don't know what document that is, but my recollection is that it was all embodied in one agreement.

Q. I want to find out whether we have it in the record here. I show you Exhibits 14 and 15. Do you refer to either of these as the extension agreement, or do you refer to some other document, as that seems to be an original agreement, isn't it? That is what year, 1924, 1925? That was an original agreement? Not an extension. That was after 1943.

Mr. Acet: There is not anything that can be misunderstood. For that reason, I do not hesitate to speak up. I offer to stipulate with counsel that

(Testimony of A. Otis Birch.)

from year to year various extension agreements were entered into between Mr. and Mrs. Birch and the Hopkins, up to 1934, extending the time to meet the contracts which are in evidence here, and thereafter extension agreements were entered into by the corporation with the Hopkins.

Mr. Crouter: Mr. Acret, I am not able to stipulate that to you, because, as you know, I do not have copies of such documents. I do not know what the facts are. I am attempting to establish the facts. I appreciate your offer nevertheless.

Mr. Acret: I think they are in evidence as exhibits.

The Court: If counsel knows whether they are in evidence, indicate now what it is, so we can save time. [192]

Mr. Acret: Counsel was one of the attorneys in the other case.

The Court: If either counsel is sure such documents are in the record now——

Mr. Acret: I know we had them in Court.

Mr. Crouter: I don't believe they are in evidence in this case.

Mr. Acret: No, but I think they were in the other case, or were available for counsel's inspection in the other case. I remember that.

Q. (By Mr. Crouter): Mr. Birch, will you please tell the Court under this option, which was given about March, 1943, what, if any, provisions the option contained as to who would own the bonds

(Testimony of A. Otis Birch.)

of the Reclamation District if the option was exercised?

A. The purchaser would.

Q. Would own all of what bonds?

A. All of the bonds of the district. I personally guaranteed with them that I deliver all the bonds and we were contemplating then dissolving the Birch Securities Company and, therefore, the bonds would come back into Mrs. Birch's hands and to me, 51 per cent to Mrs. Birch and 49 per cent to me.

Q. As I understand it, that option was exercised?

A. Yes. [193]

Q. When? A. July the 1st, 1946.

Q. Who held the bonds during that period the option was outstanding, particularly at the end of the fiscal year 1944?

A. By that time, I believe, the dissolution had practically been completed and Mrs. Birch and I owned the bonds.

Q. Do you refer to the one million five hundred ninety-four thousand dollars worth, or did you and Mrs. Birch, at the end of 1944, fiscal year 1944, acquire more than that amount of bonds?

A. Yes, we acquired more. We purchased some more of the Hopkins bonds at that time.

Q. Now, our stipulation shows, I believe, although it speaks for itself, that even way back in these early years you had an agreement to acquire from the Hopkins sisters all of their three hundred ten thousand dollars worth of bonds, didn't you?



(Testimony of A. Otis Birch.)

A. That was the balance of 786 bonds they originally had and received in 1925.

Q. Did you ever reacquire all of the three hundred ten thousand dollars worth of bonds from the Hopkins sisters?

A. Yes. We completed that transaction in 1944.

Q. Completed it in 1944? [194] A. Yes.

Q. Now, referring to a few of the bonds which were outstanding, was Lula Minter a relative of yours in any respect? A. Yes.

Q. What was the relationship?

A. She was a cousin.

Q. Had she held a land interest in any portion of that? A. What?

Q. I say, did she hold it at the very commencement of the reclamation district? A. No.

Q. Well, how did she first acquire any interest in land or bonds?

A. She didn't acquire any interest in land, but she purchased ten thousand bonds. She had previously loaned me money and I paid the loan by giving her those bonds.

Q. Did she ever receive any of this interest from the county treasurer, if you know, or did she merely use coupons to turn in?

A. That is the way she would get the interest, wouldn't she?

Q. Her coupons were actually turned in?

A. Yes.

Q. Now, referring to this, was the Republic

(Testimony of A. Otis Birch.)

Life Insurance Company—you were an officer of that corporation, too, [195] were you not?

A. Yes.

Q. What was the nature of that corporation's business?

A. It was a life insurance company.

Q. Was money borrowed from the company and then bonds held by it as security?

A. No. It purchased bonds outright.

Q. What year was that?

A. About 1927, the date that it purchased the 86 bonds.

Q. Now, up until the time when you actually reacquired these Hopkins bonds, you at all times had an agreement—I mean you and your wife—had an agreement to repurchase those bonds from the Hopkins sisters. Isn't that right?

A. Yes. They kept the original contract alive by these extensions.

Q. Were a large number of bonds, we will say something in excess of a million dollars worth, face amount, held by certain trustees, pending the payments by you and your wife for those Hopkins bonds? A. Yes.

Q. So, that is where the bulk of your bonds were held, we will say, during several years prior to 1944?

A. Well, they were in trust, and in 1934, when the Securities Company was organized, the bonds still remained in trust. [196]

Q. As I understand your testimony, before 1934,

(Testimony of A. Otis Birch.)

before you had any Securities Company or Birch Ranch & Oil Company, you and Mrs. Birch owned some of the reclamation bonds directly and held them personally. Was that the situation then?

A. That is correct. We held all of the bonds when they were originally issued, except the 786 that were held by the Hopkins for their interest in the ranch property.

Q. The Hopkins girls, their original name was Smith, was it not?           A. Yes.

Q. And they were sisters?           A. Yes.

Q. And they married two brothers?

A. That is correct.

Q. And the brothers' name was Hopkins?

A. That is right.

Q. Then, the Hopkins girls referred to, as such, were your nieces, were they not?           A. Yes.

Q. So, then, the Hopkins gentlemen, their respective husbands, were your nephews by marriage. Is that the situation?           A. Yes.

Q. Just so the Court gets the background of this picture. Then to start off——

Mr. Acret: Just a moment. Is there any insinuation [197] about that? Is it necessary to go into all of these dealings, the harshness, the feelings of the Hopkins and Birch over a period of twenty years? Counsel knows the facts of how hard these people were, and Mr. Hopkins testified in the former case that, as far as he was concerned, the bonds had to be paid and the contract had to be paid to the latter and promptly.

(Testimony of A. Otis Birch.)

Mr. Crouter: He has answered the question.

Mr. Acret: Tax cases shouldn't be tried like a criminal case, by insinuation or innuendo. I don't think it is high class.

The Court: The Court will give such effect to the testimony as it feels it deserves.

Q. (By Mr. Crouter): Mr. Birch, referring to the agreement here, dated January 10, 1925, which apparently was between you and Mrs. Birch, the first parties, and Louise Smith Hopkins, the second party, this being Exhibit No. 15 in the case, if your Honor please, I notice this was marked on the face of it, "Cancelled" and below that the name "Louise Smith Hopkins, March 15, 1944." Please tell the Court what, if anything, was done in addition to this document, with respect to any cancellation.

A. On this date or just prior to it, we paid them \$260,000.00, the balance of the \$310,000.00 that we owed them under the original contract.

The Court: How was that paid? [198]

The Witness: In cash.

Q. (By Mr. Crouter): By "them" do you refer to Louise Smith Hopkins and also Ruth Smith Hopkins, whose names are on Exhibit 14?

A. Yes, sir.

Q. Now, the Hopkins sisters had an interest in the land, to begin with, that they had acquired from their parents, I suppose, is that correct?

A. No, not at all.

Q. They did have an interest in some of the land prior to the organization of any reclamation district, did they not?           A. Yes.



(Testimony of A. Otis Birch.)

Q. And one or some of the agreements you had with the Hopkins sisters provided that you, personally, or Birch Ranch & Oil Company would purchase from the Hopkins sisters all of their land in that district. Isn't that correct?

Mr. Acret: That is objected to. The agreements speak for themselves. They are in evidence. Also, the stipulation as to facts speaks for itself. The witness' conclusion on it is immaterial.

Mr. Crouter: I haven't had a chance to read all of this. Do you mean Exhibits 14 and 15?

The Court: If they are in evidence, it is not necessary to go into it again. I thought counsel was simply using that as a predicate to another question. [199]

Mr. Crouter: I am getting back to another question.

Mr. Acret: I am referring to Exhibits 14 and 15, yes.

Mr. Crouter: I believe he could state that.

Q. (By Mr. Crouter): Was that the fact of the matter, that the agreements, Exhibits 14 and 15, provided that you and Mrs. Birch would acquire all of the interest that any of the Hopkins sisters had in any and all of the lands which was included in the reclamation district?

Mr. Acret: Just a moment. I don't think it is particularly dangerous, but it is always a poor practice, I believe, to take an agreement that is ten, twelve, or fifteen pages, and seek to interpret it.

(Testimony of A. Otis Birch.)

The Court: I will ask counsel, is there any controversy about that fact?

Mr. Crouter: Not so far as I know, but I do wish to establish whether the Hopkins had any other land.

The Court: What is the materiality of this witness saying it is in there again, repeating it orally.

Mr. Crouter: I withdraw the pending question.

Q. (By Mr. Crouter): Please tell the Court whether it is a fact that you had an agreement with the Hopkins sisters to purchase from them any and all bonds of the Reclamation District which might have been held by them, that you would purchase the bonds, as [200] well as the land, from them.

\* Mr. Acret: That is objected to as not the best evidence. The agreements which are in evidence, I think Exhibits 14 and 15, speak for themselves.

The Court: If the exhibits show, the Court is not going to permit the subject to be explored by oral testimony, if it is already in evidence.

Mr. Crouter: I will cover it now and at noon I will read the document.

Q. (By Mr. Crouter): Were there any bonds or lands, which in any manner related to the reclamation district, which the Hopkins sisters owned, the purchase of which was not covered by any other writing except Exhibits 14 and 15 before you?

A. And the extensions made from time to time after the time would have run, which was 1935, the date that the last purchase would have become due,

(Testimony of A. Otis Birch.)

having agreed to purchase ten per cent of the bonds, beginning 1926.

Q. Were those extensions in writing or just orally?

A. A very exacting written agreement, after consultation with their attorneys, and persuasion of granting of an extension.

Q. Now, I take it, from your testimony, that none of the bonds of reclamation district were actually retired at any time prior to the conclusion of any and all dealings with the Hopkins [201] sisters. Is that correct?

A. Any bonds retired due us?

Q. Retired and paid off and cancelled by the county treasurer?

Mr. Acret: That is objected to as calling for a conclusion. The witness wouldn't know the effect of the refunding issuance of the refunding bonds.

Mr. Crouter: Let's let him answer; find out.

Mr. Acret: That is quite important, your Honor, when the law of California permits repayment of a first issue and expressly provides, by a special act, for a refunding issue of these reclamation bonds. I don't think it is proper for a witness to be asked to form a legal conclusion.

The Court: The witness isn't required to do that. Any transaction that occurred, with which this witness is familiar, he might testify, but the effect of it would not be binding upon the Court.

Mr. Acret: It is our contention, your Honor, that Act 2480a provides for refunding, and that refund-

(Testimony of A. Otis Birch.)

ing issue is a repayment and the law expressly contemplated that be done in that manner.

The Court: Well, the witness can't impeach the law or interpret the law for the Court. The Court will have to do that.

Mr. Crouter: If your Honor please, what I would [202] like to know from this witness, and all I am asking him, and your Honor appreciates that both of us, it seems to me, all of us are working in the dark a little bit, because we do not have complete written records of what was done. Now, the question is whether any of the bonds, the principal of the bonds, was actually paid back to any holders by the Birch Ranch & Oil Company, and that is my question to Mr. Birch right now.

The Court: Does he know that or not?

Mr. Crouter: I believe he should.

The Witness: Yes, I know.

The Court: What is the answer?

The Witness: No, if there had been any redeemed, there wouldn't be a refunding issue for the full two million face value.

Q. (By Mr. Crouter): Please tell the Court whether that was still the situation at the end of the fiscal year 1944, that no principal amount of the bonds had ever been paid back.

A. No.

Q. That is the way it stood?

A. Yes.

Mr. Acret: I move to strike that as immaterial. Under the new refunding issue, none was due. So, it is immaterial. [203]

The Court: He can state what his opinion was.



(Testimony of A. Otis Birch.)

If it is in conflict with the law, the law would show, and not his opinion.

Mr. Acet: I think my objection of record, as I go along, would be helpful to the Court later on.

The Court: Yes.

Q. (By Mr. Crouter): Mr. Birch, I will not attempt to read to you various provisions of the California law, but I would like to ask you whether at any time there was any default in payments of principal as required under any first bond ever declared by any state, county, or reclamation authorities, and any foreclosure on the property ever instituted by any official body?

A. They instituted an action by the Postal Union Company to collect on those 86 bonds, but the settlement was made with them, so that the action was dismissed.

Q. But there was never any default declared by any state authorities, as I understand it. Is that correct?

A. No.

Q. You mean that is correct?

A. That is correct.

Q. During the year 1937, up until about the middle of 1943, did I understand you to say that these calls and assessments that you referred to, as such, by the county treasurer, were still made during that period? [204]

A. No, I believe they were not. There might have been one in 1937, but not subsequent to that.

Q. Well, was there any particular reason why they were not, besides what you have told the Court,

(Testimony of A. Otis Birch.)

I mean, any agreement or anything in writing between the corporation, Birch Ranch & Oil, and the county treasurer?

A. No, there wasn't any agreement or anything that I know of, except on general principles; both the county assessor in Yolo County and other counties tried to cooperate with the landowners, to enable them to live, and at the same time the county collect some taxes. I know the taxes, as far as the county assessor is concerned and the county tax collector, they made the five-year payment plan and the ten-year payment plan.

The Court: Ad valorem taxes, you are speaking of, five-year payment plan?

The Witness: Yes.

The Court: They couldn't pay their ad valorem taxes?

The Witness: Couldn't pay the land taxes in the extended time, but would pay—would pay interest on the current payments.

The Court: Is that taxes on levy districts or is that the general state taxes?

The Witness: That was the general state taxes, but I am merely reciting that as a comparison. It might have been [205] the same thought in mind with the county treasurer, that he wasn't going to assess land or make calls when he knew the property owners couldn't pay.

Q. (By Mr. Crouter): I suppose then, in 1943, there was a large amount of unpaid and overdue money, whether you call it taxes or interest, due on

(Testimony of A. Otis Birch.)

bonds that were payable, which sums were payable to the county treasurer, according to the records?

A. Yes.

Q. That was the real situation? A. Yes.

Q. But the county was not doing anything about that, as far as foreclosing on the land, was it?

A. No, they didn't foreclose. If they hadn't made any calls, there wasn't anything in default, no action taken.

Q. You had to have a call by the county treasurer before there was any default?

A. And the sale of the land, in the absence of payment of the call.

The Court: First a call, then a default, then a sale?

The Witness: Yes, sir.

Mr. Acret: Your Honor means in event of failure to respond to the call. Is that what Your Honor means?

The Court: Yes. [206]

Q. (By Mr. Crouter): Are you able to tell the Court what periods the amount of interest, as reflected by Exhibits 9, 10, 11 and 12, referred to, when these checks were issued here and payments were made, as shown by these exhibits. What I mean is, was that current interest or interest or taxes, or did it relate to 1940, 1942, or what period did that relate to, if you know?

A. I believe the first call made after that deferred call took place was to cover coupons that had matured. After those coupons, all past due

(Testimony of A. Otis Birch.)

coupons, had been redeemed, then regular calls were made for the current accumulation and maturity of the interest on the bonds.

Mr. Acret: I didn't object to this. I didn't examine this witness, your Honor, on that matter, because I didn't know he had any familiarity with it. Mr. Landrum was the one put on with respect to those payments, since he is the bookkeeper.

Mr. Crouter: I believe it is a part of the general picture.

Mr. Acret: I think the witness has answered it, but I believe he is out of his field, the purpose for which he was put on the stand.

Q. (By Mr. Crouter): Referring to Exhibit No. 12, Mr. Birch, and the reference here in the attached document of August 14, 1944, [207] reading as follows: "Payment to cover the unpaid portion of Call No. 21, dated December 1, 1935, together with penalty thereon, R. E. C. Dist. No. 2035, \$37,325.28." Now, that indicates to you, does it not, Mr. Birch, that the call then was for amounts which, according to the records, apparently were due as of certain prior years?

Mr. Acret: That is objected to as argumentative; calls for a conclusion of the witness. The document speaks for itself.

The Court: I think the document would be the best evidence.

Q. (By Mr. Crouter): Referring to Exhibits 9, 10, 11 and 12, Mr. Birch, please tell the Court whether it made any difference to the actual ranch



(Testimony of A. Otis Birch.)

operations of Birch Ranch & Oil Company, during the fiscal year 1944, whether those payments were made or not. I mean, could you still operate the ranch, and so forth?

Mr. Acret: That is objected to as argumentative.

The Court: What is the materiality of that question?

Mr. Crouter: I want to know whether this was a necessary condition to operation in any manner, either by any court proceedings or official demand of a county tax collector, anything of sort; whether there is any other reason for making the payments at this particular time.

Mr. Acret: Section 23 C2E, I think it is, provides for deductions for interest paid to meet local benefits on assessment bonds, and I think the law speaks for itself, and the call shows what it is for. It seems to me those four documents cover the whole case, combined with the law of the reclamation act.

Mr. Crouter: I will withdraw the pending question.

The Court: It is withdrawn.

Q. (By Mr. Crouter): Mr. Birch, you testified before Judge Turner in the prior proceeding, which has been referred to here, in April, 1943, did you not?      A. Yes.

Q. Do you recall at that time there was a question involved as to whether the ranch was on the accrual or cash basis of accounting?

A. That is correct.

Q. Please tell the Court whether after that pro-

(Testimony of A. Otis Birch.)

ceeding had been heard by Judge Turner, and the case was decided, you then held certain conferences with your representatives and decided that there was a question of the ranch being on the cash basis of accounting, you would then make actual payments to the county treasurer, and by "you" I mean the Birch Ranch & Oil Company. Isn't that one of the reasons those payments were actually made in 1943 and 1944?

A. No. The reason we paid them was because we were able [209] to raise the funds to pay them. Prior to that time, during that depression of about from 1931 to 1933, we didn't even operate the ranch and couldn't pay the taxes, the county taxes, I mean to say, and we were unable to refinance our obligations to raise any funds to apply on taxes, either the county, to the county tax collector, on the land or the assessment on the reclamation district.

Q. Very well. Please tell the Court what the facts were, whether it is not true that you did on certain occasions make arrangements to borrow money from one of the California banks, perhaps of Sacramento, and get a certified check or several checks that would be payable to the county treasurer, and actually paid to the county treasurer, and then at about the same time you would secure another check or several checks from the county treasurer, representing payments of this tax exempt interest, and that check from the county treasurer went back to the bank, paid for money which you had borrowed.

(Testimony of A. Otis Birch.)

Mr. Acret: That is objected to as immaterial.

The Court: I will overrule the objection. If he knows, he may answer. Did that happen, as has been detailed to you by the question?

The Witness: I don't recall borrowing money of a bank temporarily to pay an assessment.

Q. (By Mr. Crouter): Would you say that never happened? [210]

A. Yes, I would say that the loans that we got from the bank were for the operation of the ranch or for some other purpose, and not for the purpose of paying an assessment.

Q. (By Mr. Crouter): What was the situation as to whether all amounts due on any bonds, according to their terms, were all paid up prior to the transactions you have mentioned with Mr. Rasmussen and the Woodland Farms, Inc. Were any and all payments made paid up prior to the transaction with Mr. Rasmussen?

A. All of the coupons, I believe, were paid, but the bonds hadn't been paid for in full to the Hopkins.

Q. I mean, with respect to amounts due the county treasurer, under the interest on bonds or taxes on bonds, as you have referred to, were all of those amounts cleared up of record at the time the option was exercised and the deal was cleared out with Mr. Rasmussen and Woodland Farms?

A. I can't recall the exact date when all the arrears of past due coupons were taken up. I know

(Testimony of A. Otis Birch.)

they were completed in 1944, but whether it was completed in 1943, I wouldn't be able to say.

Q. Do you recall, in June, 1946, there was one payment or there were several payments aggregating \$474,272.53 paid to the county treasurer, and at about the same time there was one check or there were several checks aggregating \$480,000.00, [211] which were paid by the county treasurer back to the holders of bond coupons?

A. That was closing up everything that was due and past due, going out of this sale under the option.

Q. Did the Birch Ranch & Oil Company——

Mr. Acret: Just a moment. If that is subsequent to September 30, 1944, it is immaterial. I move it be stricken, because the date is not shown.

Mr. Crouter: I believe it is relevant and material. We are concerned with this whole picture.

The Court: I will overrule the objection. It is already in evidence.

Mr. Acret: I am making these objections, your Honor, so that issues won't be injected that will unduly extend the proceedings.

The Court: The Court doesn't want to extend beyond what is absolutely necessary, because the record is large enough now. I trust counsel will help to hold it down.

Mr. Crouter: Yes, I will endeavor to do my best, if the Court please.

Q. (By Mr. Crouter): Mr. Birch, do you have with you any official documents from the Commissioner of Internal Revenue relating to any accept-



(Testimony of A. Otis Birch.)

ance of a prior return or any adjustment of a prior return with respect to this question of interest deductions? [212]

A. I haven't anything personally.

Mr. Crouter: Perhaps, your Honor, counsel can show me something on that.

Mr. Acret: I think we put in a letter of about 1931.

Mr. Crouter: During the noon recess, I will be glad to see what we have.

The Court: Yes, during the noon recess, check on those things, if you will.

Q. (By Mr. Crouter): Referring to your testimony that you had no intention at any time to avoid taxes, please tell the Court whether it is a fact that in connection with your original organization of the Reclamation District, you did understand and have the intention of receiving from the county treasurer these various amounts of so-called tax exempt interest. A. My original understanding——

Q. Yes, whether you were informed of that and that was naturally a part of the original plan, as you started out, and a part of the plan as it actually operated?

A. I know that is provided for in the statutes of the state, that if bonds are issued, they will be tax exempt, but that didn't enter into this thing of organizing a district for the purpose of receiving bonds. It was represented to me by the Reclamation Board that if we performed this work——

Mr. Acret: I ask the witness be instructed to

(Testimony of A. Otis Birch.)

answer [213] the question, and not inject other issues.

The Court: Don't get off into some other question.

Mr. Crouter: I just wanted an answer to the question. I asked, as best you can, but give us whatever explanation you want to make.

The Court: He was explaining he understood the law, but that didn't induce him to take this action, as I understand. [214]

Q. (By Mr. Crouter): Please tell the Court what, if any, reason there was for not paying off any part of the principal amount as the first bond became due, as they were originally issued.

A. We didn't have the funds and it was a common practice for all districts to refund bonds from time to time.

Q. That is, just reissue other bonds?

A. Yes. That is provided for.

Q. Well, in 1935, your first bond became due, didn't it?      A. Yes.

Q. That is, the principal as well as interest?

A. Yes, and we were under quite a depression then yet. We hadn't recovered at all, and could not meet the payments and, therefore, the only alternative was to have a new issue.

Q. Do you have any balance sheets or financial accounts of your corporation for these various years, so we could see exactly what the financial condition of Birch Ranch & Oil Company was during each of these years?

A. No, I am not the bookkeeper. I couldn't read them if I had them.

(Testimony of A. Otis Birch.)

Q. You have not brought anything of that sort to the Court? A. No.

Mr. Acret: When Mr. Landrum was here, I believe he stated he had the books with him. He was the bookkeeper. [215]

Mr. Crouter: I don't recall any such. I believe that record speaks for itself, anyway.

Mr. Acret: Yes, and I am having it speak further, and I believe I stated the books were available for counsel's inspection. Further than that, if he desires Mr. Landrum to be back with them, he only has to so state.

Q. (By Mr. Crouter): Mr. Birch, have you ever added up the total amounts paid to the County Treasury by Birch Ranch & Oil Company, or by anyone on behalf of that company, as amounts of interest or taxes on these calls or assessments?

Mr. Acret: That is objected to as argumentative, your Honor. It is obvious that the accruing interest is the fixed amount, six per cent a year on two million dollars, whatever number of years it is, and besides that, it is immaterial, irrelevant, and tends to prove nothing. He has to pay whatever the law requires.

The Court: The Court didn't get the question. Will you read the question, Miss Reporter?

(The question was read.)

The Witness: No.

Q. (By Mr. Crouter): But, as I understand, your testimony is that any and all payments which

(Testimony of A. Otis Birch.)

were made were merely on the call for interest or taxes, and that none of that related to any payment [216] of principal amount of bonds.

A. No, nor didn't include any expenses, other expenses of the district.

Q. I believe our stipulated facts show that those other expenses of operating, and so forth, were paid and handled by the ranch itself?

A. Yes, but if we had to set up a set of books to operate the district and employ an office force and draw salaries on the administration of the affairs of the company, we would have created an additional cost, and that would result in additional bonds being issued to meet the costs.

Q. Now, referring to your testimony about your intentions when this reclamation district was first organized, I suppose you had some legal advice from this legal firm of Armfield & Eddy with respect to the tax phase of that matter, did you not, Mr. Birch?

Mr. Acret: That is objected to, counsel, as assuming something not in evidence.

The Court: Ask him if he had; not assuming.

Q. (By Mr. Crouter): That is my question: Did you?

A. No, I didn't have the details taken care of. We had this Mr. Conaway and Mr. Hopkins, who were active members in the ranch. Just what they conferred with the attorneys, I don't know. [217]

Q. Did you, yourself, receive any advice from any attorney or accountant with respect to the tax



(Testimony of A. Otis Birch.)

phase of that matter, prior to the organization of any reclamation district?

A. No, and, furthermore, we didn't have any thought in mind of ever getting out a bond issue.

Q. How did you learn of the tax exempt phase of that matter, if you can recall, back when it first came to your attention? That was a matter of State law, of course, but when did that first come to your attention?

A. After we received the bonds in 1925.

Q. You did not know of it, then, before that time? A. No.

Q. Referring to some of your testimony on direct examination, by Mr. Acret, with respect to the time that you waited either for money for the work that you did, or for something else from the district, it is true, isn't it, that you never did receive any money from the Reclamation District for the work either you did individually or Birch Ranch & Oil Company had done on the land?

Mr. Acret: Just a moment. That is objected to as argumentative, immaterial, your Honor. The statute provides that the County may pay in the warrant. That is the same as money, and it is immaterial.

The Court: He can state what he did, whether he received cash or warrants. [218]

Q. (By Mr. Crouter): So that you will understand, I am referring to a question which, as I recall, was: "How long did you wait for your money

(Testimony of A. Otis Birch.)

for the work that you and Mr. Conaway did in improving the district?"

I want you to tell the Court whether you ever received any actual money from the County or Reclamation District for that work.

A. I never received any money. I understood at the time the question was put, "Did we have any settlement," and the settlement was the issuance of this warrant and the exchange of the warrant for the bonds that were then ready to be floated.

Mr. Crouter: I have quite a bit more to go, if the Court please.

The Court: We had better recess until 2:00 o'clock, and counsel, in the meantime, can check on the records on some of these matters.

We will take a recess until 2:00 o'clock.

(Whereupon, at 12:15 p.m., a recess was taken until 2:00 o'clock p.m. of the same day.)

#### Afternoon Session

The Court: Proceed.

Mr. Crouter: If your Honor please, with Mr. Acret's kind permission, Respondent at this time would like to call a witness from the Collector's Office with respect to a very limited matter.

The Court: Very well.

Mr. Crouter: Miss Madeleine Webb, will you please be sworn and take the stand?

## MADELEINE WEBB

called as a witness for and on behalf of the Respondent, having been first duly sworn, was examined and testified as follows:

## Direct Examination

By Mr. Crouter:

Q. I believe your name is Madeleine Webb?

A. Yes.

Q. Please tell the Court your present occupation.

A. I am a clerk in the Collector of Internal Revenue Office, in the Income Accounts Correspondence Section.

Q. Of what office?

A. Of the Collector of Internal Revenue.

Q. And that is for the Sixth Collection District of California?

A. The Sixth Collection District of California.

Q. Located right here at Los Angeles?

A. Yes, sir.

Q. About how long have you been connected with the Office in any capacity?

A. A little over four years.

Q. Please tell the Court what, if any, general knowledge you have of the records of the Collector's Office, particularly with respect to the making and keeping of records concerning payments on any asserted income and declared value excess profits taxes.

Mr. Acret: There is no question as to the lady's qualifications or the competency of this testimony.

(Testimony of Madeleine Webb.)

Mr. Crouter: Thank you.

Q. (By Mr. Crouter): I show you Exhibit 4 in this case on hearing before the Tax Court, and call your attention to the fact that this is headed "Taxpayer's Receipt" and it is for an amount of \$12,398.85.

Have you, at my request, examined the original records of the Collector's Office to ascertain exactly what those records show with respect to the question whether or not that total sum has been assessed against a taxpayer known as Birch Ranch & Oil Company?

Mr. Acret: I think that is irrelevant and immaterial, self-serving. [221]

The Court: Overruled.

Q. (By Mr. Crouter): The question is, first, whether you examined. A. Yes.

Q. Did you learn anything from the records relating to that identical amount?

A. Yes, I did.

Q. Did I understand your examination was based on the original permanent records of the Collector's Office? A. Yes, sir.

Q. Will you please tell the Court exactly what those records show with respect to the payment of any such total sum as I mentioned?

Mr. Acret: I am not making further objection.

The Court: I understand your exceptions to this testimony.

The Witness: The Collector's record does disclose that a remittance of \$12,398.85 was received in



(Testimony of Madeleine Webb.)

the Office on July 7, 1947, to apply on an additional tax for the fiscal year ended September 30, 1941, for the Birch Ranch & Oil Company.

Q. (By Mr. Crouter): Does it indicate what kind of taxes?

A. It indicates additional income and excess profit tax for the fiscal year ended July 30, 1941. This remittance was [222] received, and since there was no assessment on the Collector's records, it was deposited in the unidentified accounts, which is termed "9-D Suspense Accounts."

Q. About what date was that done?

A. That was upon receipt of same deposited in the 9-D Account.

Q. Very well. Please proceed.

A. It remained there from the time—may I explain it this way, that if this remittance—any remittance received after July 1, 1947, up to and including June 30, 1948, which is the fiscal year of the Collector's Office, a remittance remains in the unidentified accounts until such time assessment is set up on the lists to which it could be applied, and then January of 1949, it is taken from the cashier's section, that 9-D, and deposited with the Income Tax Account Section 50, where it remains until an assessment comes through to which it could be applied.

Q. Is that Section 50 Account known by any other popular designation?

A. Unidentified accounts.

Q. Did the Collector have anything which was classified as a suspense account?

(Testimony of Madeleine Webb.)

A. Yes, also called a Suspense Account, Mr. Crouter.

Q. The Section 50 Account?

A. Section 50. [223]

Q. What is the present status of the records of the Collector's Office with respect to that identical amount of \$12,398.85?

A. At the present time it is in Section 50, the suspense account, under Account No. January 501228 on the '49 list, where it will remain until an assessment is recorded on the Collector's list, and at which time it will be transferred to the assessment.

Mr. Crouter: You may examine.

Mr. Acret: No questions. You understand, your Honor, our exception ran to all this testimony?

The Court: I understand the Petitioner reserves the exception to all the material, as being immaterial and irrelevant.

(Witness excused.)

Whereupon,

A. OTIS BIRCH

called as a witness for and on behalf of the Petitioner, having been previously duly sworn, resumed the stand and testified further as follows:

Cross-Examination

(Continued)

By Mr. Crouter:

Q. I would like to show you Exhibit No. 7 in evidence, and, if your Honor please, this is the group

(Testimony of A. Otis Birch.)

of documents which relate to an election. It is headed, "In the Matter of the [224] Legality and Validity of Refunding Bonds of Reclamation District 2035 Authorized at an Election Held in Said District on December 4, 1934."

Now, Mr. Birch, I suppose you were familiar, perhaps not with the details, but the fact that proceedings such as shown by Exhibit No. 7 here were being instituted in court at about that time.

A. I heard of it, but I didn't attend the court session.

Q. You did not attend the court session?

A. No.

Q. One of the original or first documents there seems to be what is headed "Complaint." That is this Docket 220, filed in the County Court of Yolo County, and the caption of the proceeding seems to be: "Reclamation District No. 2035, Plaintiff, versus The Lands in Said Reclamation District No. 2035, and All Persons Owning the Same or Interested Therein, Defendants." Now, the owners of the bonds of the Reclamation District at that time,—you see, that is filed April 26, 1935—I believe you have told us about all the owners of the bonds outstanding at that time, have you not?

A. What was the question?

Q. You have told us about who owned the bonds?

A. Yes.

Q. I think the record establishes that?

A. Yes. [225]

Q. Now, referring to the parties designated de-

(Testimony of A. Otis Birch.)

endants, "The Lands in Said District and All Persons Owning the Same or Interested Therein," can you tell us, in a rather specific way, who held the deeds on all the lands that were involved there, and exactly who these defendants were, the corporations or persons involved, just thinking back at that time?

Mr. Acret: I think that is immaterial, your Honor, as to this particular proceeding.

The Court: I don't see the materiality.

Mr. Acret: There is a stipulation as to who owns the lands.

The Court: What is the pertinency of that testimony?

Mr. Crouter: Well, the purpose is to show the identity of interest, if any, between the parties to the proceedings, if the Court please. I have in mind the question which will be argued on brief, as to whether the proceedings reflected in the State Court, the first page, of course, showing a default in that proceeding, whether that was a regular litigated result and, if so, who the parties were.

The Court: The Court is not going to permit a collateral attack on a judgment. I am not going into that matter. I don't think it is proper in this court.

Mr. Crouter: May the Respondent have an exception?

The Court: Yes, indeed.

Mr. Crouter: Would your Honor permit one question [226] as to whether the Birch Ranch &



(Testimony of A. Otis Birch.)

Oil Company or Mr. Birch, individually, was a defendant in this proceeding?

The Court: Yes, that is all right.

Q. (By Mr. Crouter): Please tell the Court, Mr. Birch, first, whether the Petitioner, the Birch Ranch & Oil Company, was a defendant in this proceeding. In other words, did it own lands within that district, so that under the classification it was a defendant?

A. Yes. As I understand the Court proceeding, it would name the land in the Reclamation District and the individuals owning the lands, and the purpose of the action was to validate——

The Court: The question is whether or not the Birch Company owned any land at that time.

The Witness: All but one parcel.

The Court: They didn't own all the land?

Mr. Acret: I would be willing to stipulate that at that time it owned all but one parcel.

The Court: All right. Save time. So stipulated?

Mr. Crouter: Yes, I am glad to accept the stipulation.

Mr. Acret: That doesn't, however, waive my objection that it is immaterial, because it is my theory that when a street assessment is once validly put in front of my lot, if I subsequently buy some of the street bonds in that assessment, that doesn't invalidate the assessment against my lot. [227]

The Court: Yes, I understand.

Q. (By Mr. Crouter): Now, Mr. Birch, our stipulated facts indicate that there were about 21,000 acres in the assessment, or the Reclamation

(Testimony of A. Otis Birch.)

District. That was back at an earlier stage, I believe, and what I would like to have you tell the Court is the amount of land that was included in this court proceeding here not owned by the Birch Ranch & Oil Company. How extensive was it, how many acres?      A. 320 acres.

Q. Do you remember who owned that 320 acres?

A. A man whose name is Mr. Swanson.

Q. Prior to the organization of the Birch Ranch & Oil Company, who owned the land that was included in that district; who held the title to it, if you remember?

A. Originally, there were several, but as time went on, Mrs. Birch and I acquired all of the property.

Mr. Crouter: I may say, if the Court please, that since the original stipulation of facts was filed, we have, by agreement, had it numbered, so that each paragraph bears a number and the paragraphs are numbered from 1 through 25.

The Court: That is so it can be conveniently referred to.

Mr. Acret: I numbered my copies similarly, so we will be able to refer to them. [228]

The Court: Has that been done with the one placed in the custody of the Clerk?

Mr. Crouter: Yes, it has. We took that liberty, hoping it would be agreeable to your Honor.

The Court: Yes.

Q. (By Mr. Crouter): Mr. Birch, please tell the Court, in a general way, whether most of the

(Testimony of A. Otis Birch.)

land of the Birch Ranch & Oil Company was being cultivated or the approximate amount that was being cultivated, put to cultivation and growing of crops, and what amount was pasture, and so forth.

A. About half and half divided. The land in the by-pass amounted to about 8,500 acres, and in what was called the Settling Basin, that the State created, was 4,000 acres, and the ranch together, comprising twenty-one or twenty-two thousand acres. That would be almost a fifty-fifty division.

I might add, though, there were some 1,300 acres outside of the district that belonged to the ranch.

Q. Did the County Treasurer ever make any call or demand for a payment by the Birch Ranch & Oil Company of any principal amount on the bonds there?

Mr. Acret: That is objected to as immaterial. The evidence showed no principal amount came due until 1935.

The Court: I will overrule the objection.

The Witness: No, there was no call ever made for [229] retiring any of the bonds.

Q. (By Mr. Crouter): Was Mr. Swanson related to you in any manner?

A. No, not at all.

Q. Mr. Birch, do you recall whether at any time in 1943 there was any payment made to the County Treasurer in the name and by check of the Birch Securities Company?

A. No. I recall that there wouldn't be any.

Q. There would not be any?

(Testimony of A. Otis Birch.)

A. There would not be any, no.

Q. Do you recall that there was ever any mix-up between the Birch Securities Company and the Birch Ranch & Oil Company?

A. Not to my knowledge.

Mr. Crouter: I believe that is all, if the Court please.

The Court: Any further questions by Petitioner?

Mr. Acret: If your Honor please, one or two questions.

Redirect Examination

By Mr. Acret:

Q. Mr. Birch, you testified here about the Great Republic's purchase of the bonds. Do you know how they came to purchase the bonds, the Great Republic Life Insurance Company?

A. Just an investment. [230]

Q. That is, the bonds were investments for trust purposes?

A. Yes, or for deposit in the reserve of the company.

Q. You didn't have anything to do with their buying the bonds, or did you have anything to do with that?

A. I believe Mr. Conaway really delivered the bonds to the insurance company. I was on the board of directors and the executive committee of the insurance company. I knew of the purchase.

Q. What did you say, you were on the board?



(Testimony of A. Otis Birch.)

A. Yes, I was the president of the insurance company and was on the board of directors.

Q. You were not connected with the Republic Life? A. Yes.

Q. Do you know what they paid for the bonds?

A. Yes.

Q. What was it?

A. \$80,000.00 for the 86,000 par value.

Q. Now, you mentioned about agreeing to giving or having the Securities Company give Mr. Rasmussen an option to buy the bonds. Was the Securities Company in a position to get the Minter Bonds at that time?

Mr. Crouter: If your Honor please, I object to that, in that that should be shown by records of the Securities Corporation. [231]

The Court: What was the question?

Mr. Acret: Well, it is a small matter. I don't want him left in the position—I thought there was some insinuation he couldn't deliver the bonds.

Q. (By Mr. Acret): You had the Hopkins contract and the means of getting all the Hopkins bonds? A. Yes.

Q. Did you eventually get the Minter bonds?

A. We did, yes.

Mr. Acret: I think that is all.

The Court: Stand aside.

(Witness excused.)

The Court: Call your next witness.

Mr. Acret: We rest, your Honor.

The Court: Does Respondent have any further testimony?

Mr. Crouter: I just want to check my exhibits. I believe they are all in, if the Court please.

Mr. Acret: I possibly can stipulate concerning the others.

Mr. Crouter: Respondent rests, also, if the Court please.

Mr. Acret: I wonder if it would be helpful at this time to make a short summary and leave some thoughts with your [232] Honor.

The Court: It would be agreeable with the Court.

Mr. Acret: It may be helpful just to clarify some matters.

Now, your Honor, I have this trial memorandum we prepared——

The Court: Before you begin, let me say this, that, as I understand it, this case, to get the Court's idea, has been tried heretofore in some phases by Judge Turner. It was also tried by Judge Kern of the Tax Court, and when I came here, as I understood, Judge Kern had set the case back for hearing upon one issue, and one issue only, but as I understand it, since Judge Kern's hearing matters have been changed somewhat; the payment has been made, and another taxable year is also involved, which was not involved when he heard the case. Is that correct?

Mr. Acret: No, there is no change in that respect at all.

The Court: What was the issue that Judge Kern heard?

Mr. Acret: Let me review that, and that will make it straight to your Honor.

The Court: The reason I want to get this definitely, I am under the impression that perhaps this record will be one for Judge Kern's decision, rather than mine.

Mr. Acret: I don't think so, your Honor. The only question here that is involved is the Petitioner's right, when [233] you come right down to the analysis of this, to deduct for the year 1944 such moneys as it paid to the County Treasurer to cover interest on these bonds for that year.

If it can deduct it, then it has clearly—that is, the loss of some hundred and eighty-six thousand dollars, which is many times over enough to carry back to wipe out this deficiency for 1942.

The Court: Wasn't that issue also before Judge Kern?

Mr. Acret: No, sir.

The Court: What was the issue before Judge Kern?

Mr. Acret: The matter before Judge Kern was this, that between the time when we filed this petition in the hearing before Judge Kern, the Internal Revenue agent in charge made this first reaudit of the Petitioner's books, and that reaudit, on account of these four payments to the County Treasurer, which are now in evidence, totaling \$221,000.00, and as they stated in the reaudit and the field agent's report, and on account of Judge Turner's decision,—that is the findings of fact; not his decision, his findings of fact in that first case—they allowed us the

total deduction of \$221,000.00, the amount paid as taxes and they upped the loss that we showed in our 1944 return from 84,000 to 186,000 dollars.

The Court: That was after Judge Kern's hearing?

Mr. Acret: That was done just before.

The Court: You are speaking now of what came before [234] Judge Kern?

Mr. Acret: That is right; and when I got in court here, I put that in evidence, that report, and the findings of fact of Judge Turner, to identify what they were. I stated to Judge Kern that we felt then that if we were on a cash basis, we didn't have any case for 1941 and 1943, as alleged in this petition, because we hadn't made any payments during those years, if we were on a cash basis, but that we did make payments in 1944, and that the Commissioner had filed this audit and field agent's report, stating that we suffered a loss for \$186,000.00.

We asked a continuance of the case and asked the Court to take under consideration our right to deduct that loss, as determined by the Commissioner, of \$186,000.00, and he took the matter under advisement and found we were entitled to do it, if we suffered the loss.

The Court: Did Judge Kern render a decision in the matter, findings of fact, or make any conclusion?

Mr. Acret: None whatever. It is just a legal question that we were entitled to a hearing as to whether or not we, in fact, suffered that loss of



\$186,000.00, and your Honor is hearing the matter on the merits, and for the first time on the merits. So, clearly, it is a matter for your Honor's decision.

Judge Kern handled it very capably and adequately in the respects which I stated. [235]

Now, then, that being the case, when that matter was taken under consideration by Judge Kern, and at the hearing before him, I admitted that adopting the field agent's report and the agent-in-charge report, what I will call the first report, that, as to 1941, we could have no case, because we made no payment and we made no payment even in 1943.

Therefore, we didn't suffer a loss in 1943, and had nothing to carry back to 1941. So, I believe I stated in court that we were intending to pay that assessment.

Now, what the Internal Revenue agent did has nothing to do with us. We have a 90-day letter here making a deficiency assessment against us for 1941, and we have a right to pay it at any time and we did, and we did it to relieve that court of the burden of hearing what you might say is our first cause of action, so to speak, with reference to 1941, and the only one here now is the deficiency that is in this report that we brought the petition on with reference to 1943.

If these moneys that we paid to the County Treasurer are not deductible as taxes, then we didn't suffer any loss and we haven't anything to carry back.

So, the whole question before your Honor is the deductibility of this money paid to the County

Treasurer, and that is clear, and I am now ready to start in. Was there any other questions your Honor would like to ask?

The Court: I would like to hear Respondent's counsel with relation to my reference of the case and Judge Kern.

Mr. Crouter: If your Honor please, with respect to the question propounded by your Honor, I would say this, and I refer back to the original petition, if the Court please, which was filed in the case on hearing before your Honor, Docket 8720.

This is the printed petition and your Honor may observe, or the Court will, when it gets into the making of findings in this proceeding and drawing its conclusions, that as is shown at pages 18 and 19 of the original petition, there was a reference to a loss for 1944, and the allegation in sub-paragraph (i) is in part as follows:

"During Petitioner's fiscal year ending September 30, 1944, Petitioner suffered a loss in the sum of \$73,556.88," and so forth.

The Court: That is not the amount of the loss he now claims.

Mr. Crouter: No. I was going to say, if the Court please, that certain specific matters were referred to in the petition here, as to farm losses, and so forth; and then there is a further statement still referring to the year 1944, that, "In its income tax return for said year, Petitioner listed and deducted all of the aforesaid items of loss in the total sum of \$121,084.38," and so forth. [237]

Now, this question of the loss or the claimed de-

ductions on account of Reclamation District payments was not fully or clearly set forth in the petition, and I believe, with all due respect for counsel for Petitioner, and particularly for Judge Kern, it was because there was a real question as to whether the net loss carry-back issue was properly and sufficiently asserted in the petition to give rise to jurisdiction of the Tax Court, in the first place, over the year 1944; so that I am afraid that caused us all a little confusion and a little extra work, but Judge Kern did analyze that and finally came to the clause as shown by his memorandum opinion.

He apparently came to an opinion they were entitled to a hearing on the merits.

The Court: This is the first hearing on the merits with reference to 1943 tax?

Mr. Crouter: That is correct, as to 1942 or 1944. You see, the prior hearing before Judge Turner just related to fiscal years 1937 and 1939, and they particularly involved the accounting question; but I should also say that the question of deductibility on the merits was inherent in that first proceeding, but inasmuch as the decision and the conclusion was based upon the accounting phase of the case, it was unnecessary to pass upon this question of deductibility of these payments, which is now squarely before us, I believe.

That is all I have to say as to the procedural phase of it. [238]

Mr. Acret: I can supplement that just a little more, your Honor. When this petition was drawn, we were going on the theory that we were on an

accrual basis, and on that basis,—and we were alleging certain losses, but when the matter came up before Judge Kern, I confessed our liability on the 1941 deficiency assessment, and took that out of the case, but confessing the liability, and it is on that ground we paid it.

Now, these losses that are alleged in here, the reason I haven't said anything about them, your Honor, is because when we are on a cash basis, they are not of sufficient amount to do us any good. The only thing, if we are not entitled to the deduction of \$221,000.00, we are not entitled to anything. It is just to simplify it. I don't bother with these. They are no benefit to us, and on the cash basis, that is what is the benefit.

Now, then, the whole picture is shown, and correctly shown, by this first report, which is in evidence here.

The Court: Judge Turner's?

Mr. Acret: No, Judge Turner—you see, the only effect and the reason that Judge Turner's findings of fact are *res judicata* is that Judge Turner heard all that same evidence that your Honor has heard, and considerably more.

That case, I think, took probably three or four days, and he made quite voluminous findings of fact on the details of the organization of the Reclamation District, and 1,300 acres of [239] Mr. Birch and associates' lands were excluded by the County Board of Supervisors, though they asked they be taken in the district. They were not taken and some land owners adjacent, that petitioned—about half



of them that petitioned to come in, the County Board of Supervisors didn't allow to come in.

So, in the end, in addition to Mr. Birch and his associates with their lands, there were about eight other separate landowners that were taken in the district.

Judge Turner found as to those details. Then he found as to the manner in which Mr. Birch and Mr. Conway contracted with the district to do the improvements, what improvements they made and the value, and that they got the warrants, and went all through the details of it. Then he found and stated that Mr. and Mrs. Birch, between 1925 and 1934, paid, while they owned the lands in the district, except one parcel, they paid all of the assessments to the County Treasurer.

Judge Turner makes the one error that he called it "interest," and reference to the Reclamation Act shows it isn't; it is taxes. I cite in my brief the case of Little, which concerns an individual whose Reclamation District was somewhat similar, and this court determined that was a payment of taxes and not of interests, by virtue of the provisions of those Reclamation Acts.

The Court: How extensive was the hearing before Judge Kern? [240]

Mr. Acret: I imagine part of a morning. I think after we got started, when he called the calendar, I think we were the first one; maybe from 11:00 o'clock to 12:00, or something like that, of the first morning.

Judge Turner made the findings of fact that Mr.

and Mrs. Birch, in order to operate the ranch, needed a hundred to two hundred thousand a year for operating expenses, and Mr. Birch was getting along in years. Though he appears to be a man so much younger, he is a man that is getting along in years. I think he was even 70 then, or 68, and the bank wanted him to put his property in corporate form.

Judge Turner found he did that for that purpose, in order to get back credit, and there couldn't be any more legitimate purpose of any corporation than that.

Judge Turner stated that he kept out some \$600,000.00 of his property to meet his individual debts. So there is no question about alter ego here, and it is our position it wouldn't make any difference if there were.

Judge Turner also found Mr. and Mrs. Birch deducted the amount they paid from the County Treasurer from 1925 to 1934, I think it was; and said these deductions were questioned, because Mr. and Mrs. Birch received the money back from the County Treasurer as exempt interest, and in this instance the proceeding was approved. So, that is in these findings.

Now, wherein we claim that Judge Turner's findings are [241] *res judicata* with respect to this case is that they are an adjudication of the principal facts in this case, on which counsel relies that the bond issue, you might say, is a fiction. That is all. They are an adjudication of the authenticity of the organization of the Reclamation District and of the

bond issue, in addition to the adjudication that is made by the Superior Court of Yolo County.

Now, of course, as your Honor knows, those adjudications are a matter of form, but they are a matter of form that results in a valid judgment and validates a bond issue so the bonds can be safely sold for investment trust purposes, and that is the purpose of them. They are valuable, valid adjudications, and something to rely on. We have three of them here.

By the way, I would like to state that this trial memorandum of points and authorities, in view of the stipulation we have here, it is laid out in points. While it doesn't exactly meet the rules of the Court, I think in this particular instance your Honor will find it more usable than a regular brief, and I would like to submit it as our brief. I think it is laid out to be of the greatest convenience to the Court.

Our first point, "This Court has heretofore held in this proceeding that it has jurisdiction to determine herein the amount of loss, if any, which this petitioner suffered in 1944 with the view to permitting Petitioner to carry back such loss to offset the deficiency assessment for 1942 involved herein."

So, that is the first point, and answers your Honor's question right there. This hearing is to hear on the merits, if any; whether or not we suffered the loss.

Point II is that the findings of fact of Judge Turner in the former case are *res judicata* of the questions, principal facts in this case.

The third point is that the Commissioner ought to be estopped by making a report and stating that if we don't protest it, it will become final, and wherein it becomes final, we come into this court and change our whole position.

They say we are on a cash basis. Here is what they say in this report: "For the history of the taxpayer, see prior agent's report in new U. S. Tax Court Findings of Fact and Opinion in No. 109,-993." That is Judge Turner's findings of fact.

The additional net loss—now, this where they took our net loss shown on our income tax return for \$84,000.00, which your Honor has before him, and by virtue of these same amounts that are shown on the second page, and it says, "Amount allowed in this report consists of four payments in 1944 by certified checks as follows:—"

The preceding paragraph, it says, "Amount paid in current year on current calls by the County Treasurer of Yolo County, California, \$123,000.00," and that is for the current year, "less amounts previously paid, \$5,000.00, plus amount not [243] previously accrued on books but paid in the current year," and that is for old calls. It says, "on old calls, old calls didn't meet \$769.00, total \$118,-000.00." That is the findings of the Commissioner of Internal Revenue through his local agent in charge.

Then they list the changes, "amounts allowed in this report consist of four payments in this year by certified checks as follows:" and they list the checks, and they are the four checks in evidence.



Now, we have a duly appointed, qualified and acting officer of Yolo County. We must assume that. He is the County Treasurer, and when a county treasurer makes an assessment, according to law, of a tax, that is a valid tax on the face of that assessment, and for a person to have made that tax, what else could he do? If he didn't, the law will, as I will cite it to your Honor, "The County Treasurer could declare a default, the whole bond issue in default, and come down on the land of the owner against whom the unpaid assessment was made and put the land up at public auction."

In fact, under the law he is obliged to do it. He would be remiss in his duty if he didn't do it.

So this case comes down to just one thing: The whole case is in those four checks, with the call of the County Treasurer of Yolo County, and Mr. Landrum said he got a call for each one of those. They were paid in response to a call from the County Treasurer, the receipts back stating it is to meet the interest on the bonds, and there it is. There is the payment of a tax, and the only thing, then, in connection with it that we need to go into further, is the question of law, and that is the provisions of the Reclamation District Act of California.

There is the Little Case, interpreting a similar Act, such interpretation being by this court.

Now, I was jumping ahead a little bit there. Our Point III was that the Commissioner ought to be estopped by the final report of the Internal Revenue agent in charge, dated December 8, 1947, wherein he held Petitioner entitled to deduct in its return

for the year 1944 assessment paid as taxes in the sum of two hundred twenty-one odd thousand dollars.

Now, the evidence shows that we paid that sum and we gave up our position, original position, in this case, in reliance on that report, and that report wasn't changed until after we did it, until after we made the payment.

In other words, the government got from us, on a position to take it, and upon which we relied, the payment of the assessment, the deficiency assessment that is involved in this case for the year 1941.

Now, there is quite a little text article on Merten's—we lawyers use Merten's—I don't know whether you judges do or not, because it certainly has wonderful textural explanations and analysis of the holdings of the United States Supreme [245] Court, and so forth, and I state the case, in support of the estoppel, I cite several cases, one of them being a United States Supreme Court case, and under a note in Merten's, it states as follows with reference to the Eichelberger case, which is a fifth circuit case, Eichelberger and Co. versus the Commissioner.

In Eichelberger and Company versus Commissioner, 88 F (2d) 874 (CCA 5th 1937), "In which the taxpayer had made a purported sale of property at a loss to another corporation, the stock of which was held by the same stockholders as the transferring corporation, and the Commissioner had disallowed the loss as not being a bona fide sale. The taxpayer accepted his ruling, and in a later year

made an actual sale to a third party, claiming the loss in that year. The Commissioner resisted the deduction on the ground that the sale in 1930 had been valid and the loss sustained then. The Court said: 'He cannot justly decide in 1930 that the sale did not realize the loss and thereby collect increased taxes, and in 1932 decide that it did realize the loss and collect taxes accordingly again. The United States got the benefit of his decision then and ought to abide by it now'."

The United States got the benefit of our giving up our position. It states in this petition in the instant case that we are on an accrual basis, and that then we didn't suffer any loss at a late enough date to be able to wipe out the deficiency [246] for 1941, and we paid it; and then having paid it, they got our \$12,000.00. We ought to be able to rely on their maintaining that position, continuing to maintain it, and that is the position that is stated in this report, and that position is this, reading further:

"The additional net loss as shown in this report is brought about by the allowance in full of amounts paid by the taxpayer in this fiscal year for assessment taxes on Reclamation District 2035."

The Court: What exhibit is that?

Mr. Acret: First report, Exhibit 1, our first exhibit, and, your Honor, listen to this: "Of amounts paid by the taxpayer in this fiscal year for assessment taxes——" that is what they call it "——on Reclamation District No. 2035. A part of the amount paid in this year covers amounts accrued on the corporation books in prior years and dis-

allowed in the prior agent's report as deductions, since the corporation is on a cash basis."

Now, we adopted that. You understand, your Honor, as far as this particular loss in 1944 is concerned, it doesn't make any difference whether it is accrual or cash basis, as I have heretofore stated, because we paid it.

You have an identical situation—we relied on that—they got the money and they ought not be allowed to change their position. [247]

Now, it is true there is no such thing as an estoppel against the Commissioner of Internal Revenue, but in these cases I am about to read, it is pointed out that there is an equivalent of it, and at least the Court will give full credit to the taxpayer's position in such circumstances, strain a point, to say the least.

Here is what the Court says with reference to a somewhat similar situation in Sugar Creek Coal & Mining Co., 31 BTA 344: "Even if the government may not be estopped by the conduct of the Commissioner, as a private litigant may be, and even though it is not bound by an erroneous interpretation of the law by an administrative official, the conduct of the parties to a controversy, including the conduct of the representatives of the government, is entitled to weight where questions of reasonableness of method are involved; and the conduct of the representatives of the government may be such that the Court will resolve doubts in favor of the taxpayer."

That is what I am talking about; when the Com-



missioner takes a position and adopts Judge Turner's opinion and calls this a payment of taxes and says it is deductible and gives us a loss, and on that basis we fall in with it and make the payment, the doubt ought to be resolved in favor of the taxpayer.

That isn't asking too much. I don't mean this to be as harsh as it sounds.

In quoting from Justice Holmes, in the case of *Howbert* [248] versus *Penrose*—that is when Mr. Justice Holmes was in the Circuit Court, the first circuit, 38 F (2d) 577, he says that the government "ought to turn square corners when dealing with its citizens."

It sometimes is appropriate and sometimes, when we represent taxpayers, we find that it gets to be a pretty harsh pulling against us, and this is one of the cases that invokes a little help from your Honor, it seems to me. I believe that it will.

Now, so much for that, on the *res adjudicata* and on the question of estoppel. I believe they are the equivalent of estopped, to take a position different than that in the report.

Now, we have proven just what they found in that report, and we have proven again just what Judge Turner found, and that being the case,—by the way, our Point IV here is the point that the assessment of lands for reclamation purposes is a species of taxation, and I cite a California case. That is just preliminary of what I am going to take up here under Point V, and that is that not only as is set out in the report, but Petitioner, in fact, paid the two hundred twenty-one thousand

to meet taxes of the district, and that if they did, that is a deductible item under Section 23 (c-1) E, such payments are properly deductible as taxes accrued for local benefits properly allocable to interest charges.

In other words, taxes paid for local benefits are an [249] exception and not deductible, but the taxes to meet interest on those local benefits is a proper deduction, and there is a regulation of the department there, Regulation 103 Section 19.23 (c) 3, "Assessments under the statutes of California relating to irrigation, and of Iowa relating to drainage, and under certain statutes of Tennessee relating to levees, are limited to property benefitted, and if the assessments are so limited, the amounts paid thereunder are not deductible as taxes.

"The above statements are subject to the exception that insofar as assessments against local benefits are made for the purpose of maintenance or repair or for the purpose of meeting interest charges with respect to such benefits, they are deductible."

That was what was involved in the Little Case, and they were deducted there as interest and they held they were deductible as taxes. So, that covers that.

Now, the question comes up, which counsel was talking about here, Mr. Birch taking it out of one pocket and putting it into the other. As I pointed out to your Honor, what would appear here, what intervenes is the County Treasurer of Yolo County, and he is obligated to intervene under the Laws of the State of California; so it isn't out of one pocket

into another, but it is through a public agency.

I have on my Point VI here that "The Reclamation District in California is a public corporation for municipal purposes," [250] and I have a citation on it. I think none should be necessary, because it is obvious. It is a municipal corporation, the same as any other, the county; the same in the sense that a street assessment district is.

A thought occurred to me, your Honor, and I hope I am not overdoing myself here or wearing the Court out, but the thought occurred to me there when I spoke up during the course of the trial.

Suppose I owned a lot where there was a street improvement and a street assessment was put in there and a bond issue was put against it and they have proceedings to determine the validity of them. The Court finds them valid and they sell the bonds out to a bank or something and go to the general members of the public. It is a valid street assessment district and it is a valid bond issue when it is issued.

Does that street assessment district and that bond issue become invalid if I should acquire all the rest of the lots in the block, and would it become invalid if a couple of people owned those bonds and I happened to get ahold of them and buy all the bonds?

Just put the proposition. It shows the ridiculousness of it, and that is all we have involved here, and counsel injecting the idea that it was cousins or nieces,—what if it was; how does that change the picture? It is just a different attitude. [251]

When there is a chance to put a burden on a

person for taxes, and particularly a corporation, and it not only isn't fair, but it just doesn't make sense when you analyze it that way.

The next point is Point VII, the Laws of California. It has been held time and again in different cases in California that "The Laws of California are intended to encourage and coerce the reclamation of swamp and marginal lands——"

If you could see—we know in California, know what that stuff looks like up on the Sacramento River. It is a river that carries very heavy flood water and the swamp-land around it is no use for anything, for miles and miles, and the laws of California try to get the people to go in and **encourage** them to develop them, and they have this Reclamation Act.

If it weren't for that Reclamation Act, there wouldn't be any of that land developed at all; instead they are all developed.

There is one district right after another, all along the Sacramento River, down to Sacramento, and all operating under these Laws.

As Mr. Birch says, they have a bond issue. If they don't pay the first issue, there is a section of the Act that provides they can have a refunding issue, and, as he said, they all do, and the law so provides, and that is the encouragement to be held out and it was so intended. [252]

In *Miller & Lux versus Batz*, and I cite that case: "It is the policy of the State of California to encourage the reclamation of swamp and similar lands."



In the case of Western Assurance Company versus Drain District, 72 Cal. App. 68, 72, and that is a case that is cited, and it goes on to point out the necessity of developing these lands. It says, "The reason that that is so as to Reclamation Districts is because the swamp and overflowed lands of California were granted by the Federal Government to the state upon condition that the latter——" that was with reference to a big reclamation district "——that the latter would see to the reclamation of the same so that they might become suitable for the purposes of cultivation, and, as an essential of corollary that proposition, those who purchase such lands from the state so take them subject to the right, and, in deed, the duty of the state, either by a scheme immediately directed and supervised by itself through officers or agents appointed for that purpose, or by committing that duty to the owners themselves of such lands, to coerce such reclamation according to such rules, regulations and plans as may be prescribed by the state through its legislature." That is exactly what is done here and what happens is that after our government wants more taxes, instead of permitting this beneficent plan to be carried out, the Commissioner of Internal Revenue comes in now with a new position and endeavors to frustrate it. It is a question of whether [253] your Honor is going to permit it to be done. It is an application. It is the duty of the government to turn square corners with its citizens, and we are entitled—this would spoil the effect of the exempt character of those bonds. It is a left-handed way of doing it, by saying our bonds are exempt but

you can't make the deductions, and yet the law says you can make the deductions; money paid as taxes to meet interest on bonds, deductible under the Internal Revenue Code. How can they get around it? They have to get around it by insinuations of nieces and cousins, and silly things like that.

My last point is the matter of these corporations, this incorporation. That didn't change the picture and it is a peculiar thing that Mr. Birch was allowed to make these deductions until he separated the ownership of the lands and the ownership of the bonds. As soon as he did that, the Collector of Internal Revenue thought there must be something special about it, and here is a corporation set up that is really Mr. Birch's alter ego and, therefore, he can't make the deduction, though he could make it before there was any corporation. That is how the whole situation is. You take this next report, the second report. It is just straining to get other than the fact, notwithstanding the fact that counsel stipulated with me, and the fact as to the complete arms' length transaction of Mr. Birch's with the Hopkins and with all these other bond holders. The ownings of bonds over the long period of years was [254] in the hands of not only third parties in transactions at arm's length, but even hostile third parties, and there is no getting around that; those are the facts.

This field agent, in his second report, likens the situation of the Ringe case, with just absolutely no similarity. The Ringe case was where there was

one land owner that made some improvements and got some bonds issued. I think they hardly made any improvements at all, and got about two million dollars worth of bonds issued, and then used them for tax purposes, and there it was held that those bonds were a fiction, but here we have improvements worth more than the amount of the two million dollars, made by Mr. Birch as a contractor. He had a right to be a contractor for the district.

The Court: What did the improvements consist of?

Mr. Acret: We have stipulated, and Judge Turner found, they consist of something like 56 miles of canals, 35 miles of levees, 55 miles of roads. Mr. Birch deeded the lands and the right-of-way to the District, put it absolutely out of its control, just like deeding to the state. It consisted of a site for a warehouse, and I believe a warehouse in itself. The findings on it, the stipulation on it, and everything else, value for value, and the bonds in the hands, as it appears before the Court, were four independent groups of people, some of which were even hostile.

All of the bonds were dealt in in a period of years [255] as bonds at a hundred cents on the dollar, interest paid on them, forced to be paid on them, and as I think Mr. Landrum testified, even interest on interest when the interest was late. It is just ridiculous to have a second report in here, if your Honor will read it, and see what they say about the Hopkins relationship, relationship with the Hopkins, and rely on that as one of the bases

for the deduction not being proper, and what they rely on as to the District being a fiction. It is just utterly ridiculous and there is no similarity between this case and the cases that agent in charge cites there, the Ringe case.

I think, your Honor, I have said all that need to be said with respect to this. If a land owner can ever deduct the amount he pays for taxes, I should think this would be the case where he could do it. I can't think of a time when it would be more legitimate, where that amount of money has been spent and where the bonds were so generally distributed in the hands of the third parties, and in good faith.

In conclusion, I am going to say I am not a tax lawyer, except when a time comes when I have to be for clients like Mr. Birch, but this is the pleasantest tax case I have ever tried, due to your Honor's method of handling it, and I want to express my appreciation.

The Court: Does counsel for Respondent care to make some observations?

Mr. Crouter: Yes, if your Honor please, but I will [256] try to be very brief about, and I would like to know where we stand here as to the briefing question.

The Court: Before you start, we will take a short recess.

(Short recess taken.)

The Court: Will counsel for Respondent proceed.



Mr. Crouter: If your Honor please, as the Court knows, I am merely one of the counsel for Respondent in this case, and under the practice in our office, I am more or less compelled to submit the case on a written brief. I believe, in all fairness and justice to the Court and the attorneys concerned, it should be done in this type of case, so I would like to have leave to file the usual rather complete brief in this case, actually setting forth the Respondent's position.

The Court: The Court expects that to be done, and this innovation, somewhat of an innovation, of permitting a statement of counsel being made at this time, because of the peculiarity of this case, and that it has been tried before three judges, and the Court wanted to get his bearings and find out just where we are before the case is briefed. Of course, the Court will expect argument on the briefs of counsel as to its final determination if he makes it or Judge Kern.

Mr. Crouter: Very well, and with that understanding, and without waiving the right to file the usual written brief, I do not intend to launch into any exhaustive argument about [257] the case, but I would like to comment on two or three phases of it, with the Court's permission.

The Court: The Court would be glad to hear it.

Mr. Crouter: I will address myself chiefly to the points counsel has raised here.

I would refer particularly, if the Court please, to the same points made by the Respondent in the opening statement; in other words, Respondent re-

lies upon the same position asserted and stated to the Court when this proceeding was first called. I tried to be rather specific as to the various points involved and the various positions, legal positions, and contentions, upon which Respondent relies and will rely, and that is still the Respondent's position, if the Court please.

I believe that several of those positions, particularly on the question of identity of interest, the merger of interest between individuals and corporations, and the requirements of the interest statute itself are separate points in the case, and, as I see it, those are separate legal hurdles that the Petitioner must get over in order to be entitled to the deductions that the Petitioner claims, particularly for the year 1944, and I also mention again the net loss carryback statute. That has its own requirements and exceptions and limitations, and I will attempt to point out just as clearly as I can, and under separate headings, the various statutes and cases relied upon by the Respondent, and I may say that in spite of very [258] earnest and vigorous argument by my friend Mr. Acret, he has not yet convinced me at all that any of those points lack any of their merit.

I would like to call to Mr. Acret's attention, and to the Court's attention also, two matters that did occur in the proceedings before Judge Kern, which is, as I understand it, a part of the record in this case and will remain for the Court's disposition of the issues pending now.

To answer the Court's question, there were no witnesses at the hearing before Judge Kern. That was held on June 30, 1947. The transcript contains 51 pages. There were three exhibits offered and a good deal of proceedings there consisted of colloquy between the Court and counsel to determine the posture of the case and to determine what the issues were and what it required. Now, I will also like to point out, at pages 25 and 31——

The Court: The transcript before Judge Kern?

Mr. Crouter: Yes, the transcript of June 30, 1947, before his Honor Judge Kern, at page 25 in my statement before the Court at that time, I stated in part as follows, when these same questions were under consideration:

“Now, it is contended for administratively——” and I was talking about the carryback question and the tax deduction “——administratively, and has been under consideration administratively, that is not final. It is not conceded that the [259] Petitioner is entitled to those deductions as counsel said, the statutes are still open. That is still a matter for the Bureau of Internal Revenue for the prior years, 1941 and 1942.”

Then, I believe Judge Kern grasped the situation at that time, because he said, among other things, at page 31 of the transcript:

“The Court: May I interrupt again, Mr. Crouter. I am sorry to interrupt. I want to get these things straightened out. When you are speaking about the Respondent's position, you are speaking about the Respondent's position as you know it at this time,

and not with reference to the Revenue Agent's report which is referred to by Mr. Acret."

"Mr. Crouter: That is correct."

Now, my only reason for mentioning that, if the Court please, is particularly on account of the date being June 30, 1947, which, of course, was a little while before the payment was made.

The Court: What was the date of the payment?

Mr. Crouter: The 1941 tax. However, as I said, that question, if the Court please, the 1941 year, is still open and pending in this proceeding, and that may indicate the wisdom of the Congress and the people that framed the procedural provisions with respect to the Board of Tax Appeals and the Tax Court. They apparently had the view that every year before [260] the court should be kept open until there was a final decision which finally disposed of everything for these years, so the year 1941 is still in this proceeding, and as shown by the Collector's records, there has been no final assessment for that year. So anything the Petitioner has or offered or contended with respect to the merits of the 1941 tax, it seems to me is still in the case.

The Court: What was the date of the payment of the 1941 tax?

Mr. Crouter: As I recall, that was July 7, 1947.

Mr. Acret: Right after the hearing.

Mr. Crouter: Just about one week after the hearing.

Now, as to that matter, if the Court please, I would rather answer it fully on brief, this question of estoppel by a prior revenue agent's report. I



was very much interested in counsel's argument, because that is a question which very frequently and unfortunately arises, that there will be more than one agent's examination and report for a year. To me, it has all the appearance and earmarks and the actuality of setting up a straw man and then destroying him, because the Courts have held time and again, the Tax Court and the higher Federal Courts, that certainly the sovereign United States, and that is something beyond all of us, that is the country itself, is never estopped, and its rights are never lost, and they are never prejudiced by the action of some lower administrative officer in [261] the employ of the sovereign. That is a bridge which the Supreme Court and various other Courts have crossed. The Supreme Court has held that even the Commissioner himself is not estopped or bound by a prior inconsistent determination of his own, or his predecessor in office, unless that is carried out and it becomes embodied in a court decision where the doctrine of *res adjudicata* really applies or it is the subject of a final closing agreement. There is just a very limited field of exceptions to that rule, as I recall, so that it seems to me counsel is really leading himself astray when he pins too much of his case upon the first Revenue Agent's report; that we are confronted here with the issues squarely drawn in the pleadings, and also as shown by the second Agent's report, a part of which the Petitioner has offered to the Court, to show that the Commissioner finally did not pass these deductions;

he did not allow them; he disallowed those deductions for various reasons stated and for various reasons which we have submitted to the Court here.

Now, if it is agreeable to your Honor, and without going into any extending argument on the merits of this case, I would much prefer and believe I could do it more consistently on brief. However, I am prepared, and I don't care to shirk my duty. I am prepared to go. I have my prior brief, quotations, and state authorities, but I really would prefer to do it the other way if that is agreeable to the Court. [262]

The Court: It is agreeable to the Court.

Mr. Acret: Will it be agreeable to the Court—I believe our points and authorities are adequate to submit that as our brief at this time.

The Court: You mean, as your opening brief?

Mr. Acret: As my opening brief, yes. I think your Honor will find it covers the situation.

The Court: In other words, you desire to have the statement which you have made as your opening brief in this case and then let Respondent reply to that and let you reply to his brief?

Mr. Acret: Well, it was the statement I made, together with the points and authorities which I filed at the outset of the case.

The Court: In other words, you think you would be willing to waive the formality usually practiced of filing an opening brief, and permit the oral statement made this afternoon to be accepted as your brief?

Mr. Acret: Yes, your Honor, that is, assuming

that will be satisfactory to the Court. I want to do all in my part.

The Court: What does Respondent's counsel have to say?

Mr. Crouter: That is satisfactory to me. Respondent could file a reply brief. [263]

The Court: That would expedite the filing of briefs, because the Petitioner's brief would already be filed. I guess the seriatim brief, then,—how long would Respondent's counsel want in which to prepare?

Mr. Crouter: I would like 50 days, if the Court please, on account of the transcript and other briefs I have also.

The Court: Petitioner's counsel, in his statement it might be well for him to give any citation authorities. I think he did.

Mr. Acret: They are all in and I have loaned the reporter my copy of the points and authorities, and I just have one or two remarks to make in response to counsel.

Mr. Crouter: I wonder if we can establish the due brief dates.

The Court: Did you say 50 days?

Mr. Crouter: Yes, if the Court please.

The Court: What would that be, 50 days from today?

The Clerk: It will be April 6th.

The Court: And then would Petitioner want 30 days thereafter?

Mr. Acret: That is what I was going to suggest.

The Court: 30 days thereafter in which to make

his reply brief. April 6th doesn't fall on a Saturday or Sunday, does it? [264]

The Clerk: No, Wednesday.

The Court: What would 30 days after April 6th be?

The Clerk: May 6th, on Friday.

The Court: Those days will be fixed as the dates in which the briefs, respective briefs, will be filed.

Now, did Petitioner's counsel wish to add something to what he said?

Mr. Acret: Yes, if your Honor would permit.

The Court: Yes, the Court would be glad to hear it.

Mr. Acret: And that is more on this question of estoppel. I appreciate ordinarily exactly what counsel says is true, that these reports are not final in any degree, but it must be, should be kept in mind that that report is what we responded to at the time this case was called for trial before Judge Kern, and in view of its existence, and the fact alone that it took the position that we were on a cash basis, I made, I confess, the assessment, the deficiency assessment, that is involved in this case for 1941, and there was nothing before the Court at that time but that deficiency assessment, and there still is nothing, nothing any different, and we have confessed it and we paid it for 1941. In other words, there was never anything to the contrary ever entered my mind, that if we did that there wouldn't be any question but what we would be allowed to rely on this being on a cash basis, and that loss was stated in that report. It never occurred to me as



a [265] possibility that when we did that, then they would come in and make another audit. There wasn't any reason for it, never even a suggestion that would be done, and I got the surprise of my life.

The Court: How long after that payment was made before another audit?

Mr. Acret: That audit didn't come in until months after. There was never a suggestion that anything like that was going to be done. You see, that audit didn't come in until the following December of that year.

Mr. Crouter: I believe that is the date of record, isn't it, and naturally the investigation all precedes the writing up.

Mr. Acret: That may be, but the reports and investigation didn't start until afterwards, but it never entered my mind.

The Court: That report, audit, came in, the amount was increased?

Mr. Acret: The first report increased our loss from eighty-four thousand to a hundred and eighty-six, on the ground we had a right to make these deductions and that we had suffered that loss.

Then, the next report comes along and disregards Judge Turner's findings of fact to which they referred in the first report, and says just the opposite of Judge Turner's [266] findings of fact, that this is a fiction, and classed us as having a gain instead of a loss in 1944, but they state in that report, the gain, we don't pay any taxes on it because we can carry back a loss for still a later year to wipe out

that gain. They make us come out even. It was just a clever thing that made us come out even for 1944, instead of leaving us this to fall back on. That is the situation. I didn't think I would be dealt that way by the Department of Internal Revenue.

The Court: I suppose that concludes the statements of counsel and the Court thanks counsel for the cooperation and assistance in this rather complicated and difficult matter, and appreciates also the fact that the opening brief has been filed, which will expedite the consideration of the case by the Court.

I believe that concludes the docket and all matters pertaining thereto at this session, the Court at the Los Angeles setting, so we are now finally adjourned sine die.

(Whereupon, at 3:35 o'clock p.m., Tuesday, February 15, 1949, the hearing in the above-entitled matter was closed.)

Filed T.C.U.S. March 8, 1949. [267]

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[Title of Tax Court and Cause.]

## STIPULATION TO CORRECT TRANSCRIPT

It is hereby stipulated by respective counsel in the above-entitled proceeding that the transcript of record at the hearing held on February 11 and 15, 1949, may be corrected as follows:

Page 28, 17th line, change "now" to "not"

Page 32, 21st line, change "provide" to "deprive"

Page 36, last line, insert comma after "allowed" and change "They" to "or"

Page 42, 20th line, change "agents" to "acts"

Page 43, insert "every year" after "litigated"

Page 67, last line, change "collectible" to "taxable"

Page 117, second line, add "assessment" after "prohibit"

Page 138, 16th line, change "staff" to "Stout"

Page 223, 22nd and 23rd lines, change "expense" to "suspense"

Page 224, 4th line, change "expense" to "suspense"

Page 237, 21st line, change "foreign" to "farm"

Page 238, first line, change "plain" to "claimed"

Page 262, 7th line, change "where" to "or"

/s/ GEORGE ACRET,

Counsel for Petitioner.

/s/ CHARLES OLIPHANT, ECC

Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

Received and Filed T. C. U. S. May 2, 1949.

The Tax Court of the United States

B.T.C. No. 122

BIRCH RANCH & OIL COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Docket No. 8720

Promulgated December 15, 1949.

## FINDINGS OF FACT AND OPINION

A taxpayer corporation, keeping its books on the cash basis, owned substantially all land comprised in a California reclamation district. The district had outstanding 2,000 6 per cent bonds of \$1,000 face value each, payable from the proceeds of improvement taxes assessed against the land. The taxpayer and the taxpayer's sole shareholders, husband and wife, and holding companies wholly owned by the shareholders held 1,680 of the district's bonds at the beginning of the fiscal year 1944 and acquired 310 more about the middle of the year. To pay interest on the bonds, the reclamation district, through the County Treasurer, made assessment calls which petitioner paid during the year, and deducting such payments as taxes, it computed a net operating loss for fiscal 1944 which it claims as a carry-back deduction for fiscal 1942.

1. A revenue agents' report, addressed to the taxpayer, in which the tax payments were allowed



as deductions, held, not to estop the Commissioner from defending a subsequent determination that the taxpayer had no net operating loss for fiscal 1944 and consequently no carry-back, such determination being based on a disallowance of the deduction of tax payments.

2. Amounts paid on call of the County Treasurer as taxes to meet interest on bonds of a California public reclamation district, held, deductible by the taxpayer although it owned all the land assessed and its sole shareholders owned or controlled a majority of the bonds, the minority bondholders having a material number of bonds. *Rindge Land & Navigation Co.*, 2 B.T.A. 1179, distinguished.

George Acret, Esq.,

For the petitioner.

Earl C. Crouter, Esq.,

For the respondent.

The Commissioner determined deficiencies of \$7,833.44 and \$11,915.67 in petitioner's income taxes for the fiscal years ended September 30, 1941, and 1942, respectively, and deficiencies of \$4,565.41 and \$1,687.10 in declared value excess-profits taxes for those respective years. In the original petition error was assigned in the determination that petitioner's books were kept on the cash basis, not on an accrual basis, and in the consequent disallowance of deductions claimed by petitioner on account of accrued taxes, payable but unpaid, to a California reclamation district. In a proceeding involving the fiscal

years 1937 and 1939, Docket No. 109993, this Court decided like issues adversely to petitioner's contention while this case was pending, and after affirmance of that decision on appeal petitioner abandoned those assignments and amended its petition to claim a carry-back deductible in fiscal 1942 because of an alleged net operating loss sustained in fiscal 1944. The Commissioner allowed no carry-back deduction, having computed a net income of \$34,711.50 for fiscal 1944. In so doing he did not allow the deduction of taxes of \$221,610.87 actually paid to the reclamation district in that year on the ground that petitioner owned all the land of the district and it or its stockholders owned substantially all the bonds of the district so that petitioner's obligation to pay taxes and the district's obligation to pay interest on the bonds was lacking in substance. Petitioner contests the disallowance and the resulting determination that there was no net loss carry-back available as a deduction for fiscal 1942 under section 122(b), Internal Revenue Code. In a Memorandum Opinion entered March 24, 1948, it was held over respondent's objection that this Court had jurisdiction to decide the issue so raised. The case was submitted on a stipulation, which we hereby incorporate by reference as findings of fact, on oral testimony and on exhibits.

### Findings of Fact

Petitioner, a Nevada corporation with principal office at Los Angeles, California, filed its income tax returns for the fiscal years ended September 30, 1941,

1942 and 1944 with the collector of internal revenue for the sixth district of California. Petitioner was organized on October 15, 1934, by A. Otis Birch and his wife, M. Estelle C. Birch, who transferred to it a 21,000 acre tract of land known as the Conaway Ranch and certain other property. On the same date Birch and wife also organized the Birch Securities Co. (hereafter called Securities) as a Nevada corporation and transferred to it 1,594 bonds, each of \$1,000 face value, issued by Reclamation District No. 2035 (California), certain stocks and other assets. The two transfers comprised all of their property. On the same date they also organized the Birch Holding Co. (hereafter called Holding); all shares of petitioner and Securities were transferred to it, and it issued 49 per cent of its shares to Birch and 51 per cent to Birch's wife. Birch was president and in control of the affairs of all three corporations. Securities and Holding were formed for convenience and conducted no business. Petitioner operated the Conaway Ranch, raising and selling crops and sheep.

The Conaway Ranch is situated in Yolo County, California, about five miles from Sacramento. It was purchased in 1914 and thereafter enlarged by the Birch Oil Co., a partnership in which petitioner and his wife, the wife's parents, and Birch's nieces, hereafter called the Hopkins sisters, held interests. At the time of the initial purchase the Sacramento and San Joaquin Drainage District, created under the laws of California, was making surveys in the area for a flood-control project, and the Reclama-

tion Board of the state later informed the Birch Oil Co. that if it would construct a levee across the ranch adjacent to a proposed Yolo By-Pass, an assessment would be made against all lands in the drainage district to pay for the construction and for flowage rights. Desiring to develop its land, Birch Oil Co. later petitioned the Supervisors of Yolo County to create a reclamation district which would comprise the ranch, and in April 1919 the Supervisors approved the establishment of Reclamation District No. 2035. B. F. Conaway, Birch's father-in-law, C. Harold Hopkins, the husband of Birch's niece, and a local attorney were appointed district trustees. A program of improvements, estimated to cost \$2,264,740, was authorized, and commissioners were named who apportioned the cost of the improvements among lands in the district according to the benefits to be received and filed with the Treasurer of Yolo County assessments against the lands to meet such cost.

The Birch Oil Co., under direction of the district's engineer, constructed the improvements, which consisted of many miles of roadways, canals, ditches, bridges, pumping plants and other structures, at a cost of slightly over two million dollars. It financed the work, and after completion in 1924 received a warrant, dated January 5, 1925, directing that the district, through the Treasurer of Yolo County, pay it two million dollars. On January 23, 1925, 2,000 bonds of the district, each of a par value of \$1,000, were offered at auction to provide the necessary funds, and Birch purchased all of them.



giving the \$2,000,000 warrant in payment. These bonds bore 6 per cent interest payable on January 1 and July 1 of 1925 and each year thereafter on presentation of an interest coupon to the County Treasurer; 227 bonds were to mature on January 1 of 1935 and a like number on January 1 of each succeeding year, ending with maturity of the last 184 on January 1, 1943. Principal and interest were payable out of moneys collected by the Treasurer of Yolo County from assessments against the benefitted lands, which assessments were to be deposited "into the main county treasury" but "credited to the bond fund" of the district, as provided by section 3480, art. II, ch. 1, Title 8, Deering's Political Code of California.

Pursuant to a contract of 1924 Birch and wife purchased the Hopkins sisters' interests in the ranch and Birch Oil Co., and in 1926 they purchased the wife's parents' interest. By virtue of these acquisitions and the purchase of small adjacent parcels of land they came into ownership of the entire ranch, then consisting of about 21,000 acres. The ranch was co-terminous with Reclamation District No. 2035 except for 1,300 ranch acres which lay outside the district and 240 district acres which lay outside the ranch. In buying the interests of the Hopkins sisters, Birch paid them \$1,000 cash and 786 district bonds. Simultaneously he and his wife agreed to buy back from them the 786 bonds at face value in specified annual installments on January 1 of each year from 1926 to 1934, and as security for performance they placed their remaining 1,214 bonds

with trustees empowered to sell and make good any default by them on the contract. The Hopkins sisters, however, reserved the right not to sell on any installment date. During the first six years petitioner and wife paid for and received 476 bonds, as contemplated by the contract. Because of financial difficulties they thereafter ceased to purchase installments of the remaining 310. But instead of invoking action by the trustees the Hopkins sisters granted them a time extension without release from the obligation to buy. Prior to 1937 petitioner and wife sold 10 of their district bonds to Lula Minter, a cousin of Birch, and 86 to the Great Republic Life Insurance Co., of which Birch was president and a director.

During the years 1925-1930 Birch and wife paid to the County Treasurer of Yolo County on call of the assessment against the ranch the amounts necessary to meet interest payments on the bonds, and the Hopkins sisters collected their interest from the Treasurer on presentation of the matured coupons. In succeeding years Birch bought the coupons of the Hopkins sisters as they matured, and deposited them with the Treasurer, receiving a receipt and credit on the assessment against the ranch. After petitioner acquired the ranch in 1934, it too purchased at face value matured interest coupons from the Hopkins sisters and from Lula Minter, turning them in to the County Treasurer. It did not buy matured coupons on the 86 bonds held by the insurance company, and that company's successor in interest eventually brought suit to enforce collection

of interest. The suit was settled by petitioner's purchase of the 86 bonds and accrued interest in 1940 for \$65,000.

No amount was ever paid into the reclamation district by Birch and his wife or by petitioner for the purpose of paying off the bonds. But prior to maturity of the first 227 and in 1935 the original issue was refunded by 2,000 new 6 per cent bonds of \$1,000 face value, of which 50 were to mature on January 1 of 1945 and of each succeeding year. To test the legality of the original issue the district trustees filed a complaint with the Superior Court of Yolo County, and after consideration of the evidence the court on March 2, 1925, entered a decree that:

\* \* \* said bonds are a valid, legal obligation  
of said Reclamation District No. 2035, \* \* \*

The refunding bonds were likewise held a legal obligation of the district by decree entered in a similar proceeding on June 25, 1935. The proceedings were not contested.

Since organization petitioner has operated the Conaway Ranch, and has borne all costs and expenses of maintaining and operating the improvements of the reclamation district, treating such disbursements as part of its expenses in operating the ranch in a manner which would be no different if there were no reclamation district, whether formal or actual, and the district has no expenses which are not taken care of by petitioner. For its ranch operations petitioner keeps a set of books on the basis of cash receipts and disbursements.

The officials of California counties are lenient with the owners of assessed lands in reclamation districts, and while there was no express agreement, the Treasurer of Yolo County refrained, in and after 1937 from making any calls on petitioner for payments or declaring defaults or taking foreclosure action against the ranch, being aware that petitioner was in no position to pay an assessment. Petitioner nonetheless accrued on its books and deducted on its income tax returns an amount of \$120,000 a year for which a call could have been made to provide the County Treasurer with moneys necessary for the payment of the annual 6 per cent interest on the \$2,000,000 face value bonds. It continued to buy at face value the maturing interest coupons on the 310 bonds of the Hopkins sisters and the 10 bonds of Lula Minter, paying \$18,600 and \$600 a year, respectively, for them. The Commissioner allowed a deduction of the \$600 paid to Lula Minter, but disallowed the rest of the \$120,000 claimed. Petitioner contested such disallowances for 1937 and 1939 in a proceeding before the Tax Court, Docket No. 109993. The Court held that the \$18,600 paid to the Hopkins sisters was deductible, and sustained disallowance of the rest. Memorandum Opinion entered April 20, 1944, affirmed by the Circuit Court of Appeals for the Ninth Circuit on January 6, 1946, 152 Fed. (2d) 874. This decision was based on a finding that petitioner kept its books for ranching operations on a cash, not an accrual basis, and had made no payments other than the \$600 and the \$18,600.



On September 30, 1943, petitioner held the 86 bonds acquired from the life insurance company; Securities held the 1,594 transferred to it at organization; the Hopkins sisters held 310 subject to the sale contract with Birch and wife, and Lula Minter held 10. On March 15, 1944, Birch and wife bought the remaining 310 bonds from the Hopkins sisters, and before the close of the fiscal year on September 30 Securities was liquidated and dissolved. Securities had been suspended since 1938 for failure to pay a state tax. Thus at the close of the fiscal year 1944 Birch and wife held directly 310 of the 2,000 bonds of the district; Holding held 1,594 from the liquidation of Securities; petitioner held 86, and Lula Minter 10. In March 1943 petitioner, Birch and wife gave to several individuals a written option to purchase the Conaway Ranch and all the district bonds.

During the period 1937 until late in 1943 petitioner made no cash payments to the County Treasurer to provide interest on the bonds and received no call to make a payment. In 1943, however, funds became available to it, and on October 13, 1943, the Treasurer made a call for \$58,565.92, payable November 12. Petitioner advised the Treasurer that it could not pay the amount until later and would submit to a delinquency penalty. In reply the Treasurer explained that the penalty was "part and parcel of the Call," which was "for interest only." On December 28, 1943, Securities transmitted to the Treasurer coupons from 166 bonds and advised that the trustees for the Hopkins sisters would present

coupons from 1,278 bonds. It requested remittance of \$49,320 to cover the accrued interest. The following day petitioner paid the assessment call and a penalty of \$5,856.59 by its check for \$64,422.51 drawn in favor of the County Treasurer, and the Treasurer remitted \$49,320 interest to Securities on January 8, 1944. On April 10, 1944, the Treasurer made another call for \$53,721.65 payable May 10. Petitioner paid this call and a 10 per cent delinquency penalty of \$5,371.94 by its check for \$59,093.59 dated June 28, 1944. On August 12, 1944, petitioner gave to the Treasurer its check for \$37,325.28 in satisfaction of the unpaid portion of a call dated December 1, 1935, together with penalty. Before making this remittance petitioner inquired of the Treasurer by letter if the Treasurer would pay the interest coupons in arrears upon receipt of the amount. On September 20, 1944, it paid the Treasurer \$60,769.49 in satisfaction of a call dated September 8, 1944. In making calls, the treasurer computed an amount which, with any balance on hand, was sufficient to provide \$60,000 for the semi-annual interest due on the bands, and amounts paid as penalties were reflected in his computations. The four payments which petitioner made during its fiscal year 1944 aggregated \$221,610.87. Soon after the collection of money by call the Treasurer paid interest on the bonds, but no interest was ever paid without such preceding collection.

On its tax returns for the fiscal years ended September 30, 1941 and 1942, petitioner claimed a deduction of \$120,000 on account of the tax due Rec-

lamation District No. 2035; for each year the Commissioner disallowed the deduction "except as to \$19,200 paid to the Hopkins sisters and Miss Minter." After affirmance of this Court's decision in Docket No. 109993 and on July 7, 1947, petitioner paid to the collector \$12,398.85 on account of the deficiencies determined in its income and declared value excess-profits taxes for the fiscal year 1941. As there had been no assessment of the determined deficiencies, the payment was credited by the collector to a suspense account and not applied in satisfaction of a tax. On its return for the fiscal year ended September 30, 1944, petitioner claimed a deduction of \$118,890.87 as taxes paid to Reclamation District No. 2035, and reported a net loss of \$84,179.37 for the year. In a report dated January 23, 1947, addressed to petitioner, the revenue agent in charge of the Los Angeles Division recomputed a net loss of \$186,899.37 for the year, and in so doing, allowed a deduction of \$221,610.87, or the amount actually paid to the Treasurer of Yolo County on account of the district taxes and penalties. In a subsequent report, dated December 8, 1947, deduction of the \$221,610.87 was disallowed on the ground that:

\* \* \* there was no real or actual obligation outstanding against the taxpayer, since Reclamation District No. 2035 was comprised exclusively of the taxpayer's property, and since A. Otis Birch and his wife, Estelle Birch, the sole stockholders of the Birch Ranch and Oil Com-

pany hold substantially all the bonds of the Reclamation District.

\* \* \*

As the interest received by A. Otis Birch and his wife, Estelle Birch, is non-taxable, the amounts claimed as taxes paid by the Birch Ranch and Oil Company is considered non-deductible.

As a consequence of this disallowance the Commissioner determined that petitioner had no net loss carry-back from the fiscal year 1944 to the fiscal year 1942.

### Opinion

Johnson, Judge:

Petitioner charges the Commissioner with error in failing to allow the deduction of a net operating loss carry-back in the computation of its income and declared value excess-profits taxes for the fiscal year ended September 30, 1942, by virtue of a net operating loss of \$186,899.37 sustained by it for the fiscal year ended September 30, 1944. Originally petitioner also assigned as errors the Commissioner's disallowance of the unpaid portion of a deduction of \$120,000 claimed on each of its returns for the fiscal years 1941 and 1942 as accrued taxes payable by it to Reclamation District No. 2035. When the petition was filed, a similar issue was pending before this Court in Docket No. 109993, involving petitioner's right to deduct the same accrued liability of \$120,000 for each of the fiscal years 1937 and 1939. This Court's holding that petitioner's books were kept on a cash basis and that it was entitled to de-



duct only the \$18,600 paid to the Hopkins sisters and the \$600 paid to Lula Minter was affirmed by the Circuit Court of Appeals for the Ninth Circuit on January 6, 1942, as reported in 152 Fed. (2d) 874.

At the first hearing of this proceeding on June 30, 1947, petitioner, accepting the holding that its books were kept on the cash basis, conceded that there were deficiencies in tax as determined for its fiscal years 1941 and 1942, but asked the Court to provide in its order that the tax liability for fiscal 1942 be computed to reflect the carry-back of losses sustained by it in fiscal 1944. Rejecting respondent's contention that a decision of deficiencies in the amounts determined be entered without adjustment for any carry-back, this Court in a Memorandum Opinion entered March 24, 1948, took note that petitioner's right to a carry-back was properly raised as an issue and held that such issue was a proper subject for decision. Petitioner then moved to reopen the case for the purpose of presenting evidence relative to its net operating loss for fiscal 1944. This motion was granted, and petitioner thereafter amended its petition to make allegations concerning the payments made to the County Treasurer and to plead that the respondent was estopped to deny the deduction of these payments in fiscal 1944. The issue thus raised for decision requires a determination of petitioner's right to deduct as taxes in fiscal 1944 the \$221,610.87 which it paid in that year to the Treasurer of Yolo County on calls under the

tax assessment of the reclamation district against the Conaway Ranch.

In a report dated January 23, 1947, addressed to petitioner, the revenue agent in charge of the Los Angeles Division allowed the deduction in question and computed a net operating loss of \$186,899.37 for fiscal 1944. Petitioner now argues on brief that since it paid the deficiencies of \$12,398.85 determined (but not assessed) for fiscal 1941 in reliance on this report, respondent should be estopped from denying it the advantage of the carry-back deduction therein recognized as allowable for fiscal 1942, which deduction it anticipated in making the payment. The agent's first computation was reversed, however, and in a later report, dated December 8, 1947, the payment of the \$221,610.87 was not allowed as a deduction with the result that the net loss of fiscal 1944 was converted into a net income of \$34,711.50. As a consequence the Commissioner determined that there was no loss carry-back from fiscal 1944 available as a deduction for fiscal 1942.

We fail to perceive in the Commissioner's action any basis whatever for an estoppel. The amount of the deficiency for fiscal 1941 was in no wise affected by any deduction on account of a loss carry-back to which petitioner might or might not be entitled for fiscal 1942. Petitioner had no right, under the decision in Docket No. 109993, to deduct in fiscal 1941 taxes due to the reclamation district which it had accrued but not paid. It so admits by abandoning all issues relating to fiscal 1941. There was hence no issue raised for fiscal 1941 about which the

Commissioner's action could have misled petitioner, and in any event the payment was not applied to the 1941 deficiencies, which have not yet been assessed, but was placed in a suspense account.

By section 23(c) (1), Internal Revenue Code, taxes paid or accrued within the taxable year are deductible except:

(E) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges; \* \* \*

As all of the \$221,610.87 paid to the County Treasurer was for application to interest charges, none of it is excluded as a deduction by the statutory exceptions, and respondent does not contend that it was. Its disallowance was explained in the agent's second report as follows:

This disallowance is based on the fact that there was no real or actual obligation outstanding against the taxpayer, since Reclamation District No. 2035 was comprised exclusively of the taxpayer's property, and since A. Otis Birch and his wife, Estelle Birch, the sole stockholders of the Birch Ranch and Oil Company hold substantially all the bonds of the Reclamation District.

Section 23 of the Internal Revenue Code states:

Deductions from Gross Income.

In computing net income there shall be allowed as deductions:

(b) Interest—All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations \* \* \* the interest upon which is wholly exempt from taxes by this chapter.

(c) Taxes—Generally.

(1) Allowances in General—Taxes paid or accrued within the taxable year except—

(a) taxes assessed against local benefits of a kind tending to increase the value of the property assessed.

As the interest received by A. Otis Birch and his wife, Estelle Birch, is non-taxable the amounts claimed as taxes paid by the Birch Ranch and Oil Company is considered non-deductible.

Respondent, now defending the disallowance on both the above grounds, argues first that the Birches, the petitioner and the reclamation district were all one and the same in substance since petitioner owned all the assessed land in the district, the Birches through Holding owned all the stock of petitioner, and they and petitioner owned substantially all the bonds of the district. On this background he reasons that in effect the same party paid the taxes in controversy and received the tax-exempt interest



which those taxes supplied. He urges that under such circumstances the district should be ignored for tax purposes as a legal fiction, and that the tax and interest payments should be disregarded as not having any business purpose and not discharging any real legal obligation.

To buttress this view, respondent cites numerous sections of the Political Code of California, Part 3, Title 8, chapter 1, article 2, relating to reclamation districts, pointing out that section 3472 authorizes the formation of a district without the intervention of trustees by parties owning all the land affected; that section 3480 empowers the landowners of those districts which are under trustees to authorize bonds by vote; requires that 10 per cent of any bonds issued be retired within ten years of issuance; that a fund be created for such retirement; that parcels of land be sold to provide delinquencies in assessment payments; that the district's bonds may be used in satisfaction of assessments; and that section 3493 permits owners of 50 per cent of the land to dissolve the district. He concludes that Reclamation District No. 2035 was in fact if not in form a private district; that in actual operation it was treated as a private district because no assessment taxes were paid from 1937 to 1943; no sinking fund was created, and the fiction of a public district was artificially kept alive to the end that petitioner might deduct the amount which it paid as taxes and which it or its sole stockholders received back as tax-exempt interest.

The essential factual premises or inferences which respondent assumes for this argument are not adequately supported by the evidence. We can disregard as negligible the 240 district acres which petitioner did not own and against which an assessment for bond interest apparently was not made, but we can not lightly ignore a public district invested with taxing powers and other sovereign attributes and the substance attaching to the very large number of bonds which were held by parties who had no identity of interest with the Birches and whose right to bond interest was consistently observed,—in one case, after threat of suit. The Hopkins sisters acquired 786 of the 2,000 bonds in 1925; they owned 310 from 1931 to March 15, 1944, or during five and a half months of fiscal 1944. At an undisclosed date the Birches sold 86 bonds to the Great Republic Life Insurance Co., and its successor sold these bonds to petitioner in 1940; the Birches sold 10 bonds to Lula Minter who held them throughout fiscal 1944. Petitioner regularly paid to the Hopkins sisters and to Lula Minter the amount of accrued current interest due them, receiving and turning over the interest coupons to the County Treasurer. By so doing it acquired a credit in the same amount on the district's assessment for interest. See section 11, article II, chapter 1, Title 8, Part 3, Political Code of California, and hence it is not technically correct to say that no assessment taxes were paid from 1937 to 1944. An amount of \$19,200 was paid each year, and by this Court's decision in

Docket No. 109993 the amounts so paid were deductible.

Without formally pleading *res judicata*, petitioner argues on brief that the recognizable character of the district and petitioner as separate entities is in fact *res judicata* by virtue of our holding in the prior proceeding. While that decision, involving the fiscal years 1937 and 1939, would not here support the plea, if made, see *Commissioner v. Sunnen*, 333 U.S. 591, we deem the facts therein considered so nearly identical with those existing in fiscal 1944 as to require the same conclusion previously reached. To view the tax assessment as paid by the same party which received the bond interest, it is not enough to identify petitioner, Holding and Securities with Birch and his wife. It is also necessary to identify with them the reclamation district, and this district is by state law:

\* \* \* a public, as distinguished from a private, corporation. It acts as a state agency invested with limited powers, \* \* \*. [*Metcalf v. Merritt*, 14 Cal. A. 244; 111 Pac. 505]

Respondent cites *Rindge Land & Navigation Co.*, 2 B.T.A. 1179, and the very similar case of *California Delta Farms, Inc.*, 6 B.T.A. 1301, as decisions in which a similar district was for tax purposes identified with the sole landowner in it. In the former case the sole landowner, a corporation, had caused the district to issue to it a warrant for an amount in excess of the cost of property which it transferred to the district, and had used that warrant to

procure all the district bonds which bonds it gave to creditors in place of certain indebtedness of its own. The Board of Tax Appeals refused to recognize the excess of the warrant over the property as resulting in taxable gain, but in so doing, expressly confined its "discussion and decision to the particular facts." As those facts indicated that the taxpayer owned all the district and procured all the bonds, obviously no third party's interest was involved and the price named for the property was admittedly arbitrary and designed to further the taxpayer's debt refunding scheme. As the issue related only to a sale between the landowner and the district, moreover, the legal incidence of bonds and assessments was not even involved. But the intervention of even a small interest by third parties has been deemed to preclude a disregard of the separate character of a public district. In *Kings County Development Co.*, 27 B.T.A. 1291, the taxpayer's gain on a sale of property to a reclamation district was held taxable even although the taxpayer owned 80 per cent of the district land. In so deciding, the Board expressly recognized that:

\* \* \* Such districts are separate and distinct legal entities from the land owners within the district, \* \* \*.

Respondent correctly asserts that in numerous cases deductions such as interest have been held unallowable where it appeared that the payor and payee were economically identical, e.g., *Prudence Securities Corporation v. Commissioner* (C.C.A.,



2nd Cir.), 135 Fed. (2d) 340; Marian Bourne Elbert, 45 B.T.A. 685. But the decisions on which he relies do not involve tax assessments of a public corporation or interest payable on its bonds, a substantial number of which were owned over the years by parties having no identity of economic interests with the taxpayer. We have already held in Docket No. 109993 that the amounts which petitioner supplied in satisfaction of interest on bonds held by the Hopkins sisters and Lula Minter were deductible. The Hopkins sisters continued to own bonds during nearly half of fiscal 1944 and Lula Minter owned 10 during all of it. That part of petitioner's assessment payments used to pay interest on their bonds is obviously deductible under the prior decision. Should a distinction be made in regard to the tax applied to interest payments on petitioner's bonds? We think not. The funds which the district collected by its assessment calls were for the payment of interest in general, and we are of opinion that petitioner's right to deduct its payments as a tax is not defeated by the fact that a part of such payments became available to pay interest on bonds held by it, by Securities, by Holding, or by the Birches. *Andrew Little*, 21 B.T.A. 911.

Respondent argues further that the "payments of interest on reclamation bonds" was the payment of interest on indebtedness incurred and continued to purchase and carry tax-exempt obligations, and hence such payments are not deductible under section 23(b), Internal Revenue Code. Recognizing

the reclamation district as a legal entity, we view petitioner's payments as made in satisfaction of taxes, not of interest, and the argument thus lacks factual foundation. As taxes assessed for interest only, they are not of a kind tending to increase the value of the property assessed, and are hence properly deductible. *Mary E. Evans*, 42 B.T.A. 246; *Missouri State Life Insurance Co.*, 29 B.T.A. 401; *Andrew Little*, *supra*.

We hold that the Commissioner erred in failing to allow the deduction of the taxes of \$221,610.87 paid by petitioner in fiscal 1944, and that the amount of petitioner's net operating loss for that year, available as a carry-back to fiscal 1942 under the provisions of section 122(b) (1), should be recomputed to reflect such deduction. In his answer to petitioner's "Supplement and Amendment to Petition," respondent admitted:

\* \* \* a determination of a disallowance of a deduction claimed by the petitioner for the taxable year 1944 in the amount of \$221,610.87 for alleged taxes or interest paid, and that as a result of such disallowance the respondent has found and determined that petitioner had no net loss carry-back from 1944 to the taxable year 1942; \* \* \*.

As no factor of computation other than treatment of the \$221,610.87 taxes paid was put in issue, the effect of this decision is limited to a deduction of those taxes in arriving at the amount of net oper-

ating loss for fiscal 1944 and the carry-back available as a deduction for fiscal 1942.

Reviewed by the Court.

Decision will be entered under Rule 50.

Served Dec. 15, 1949.

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[Title of Tax Court and Cause.]

RESPONDENT'S COMPUTATION FOR  
ENTRY OF DECISION

The attached proposed computation is submitted, on behalf of the respondent, to the Tax Court of the United States, in compliance with its opinion determining the issues in this proceeding.

This computation is submitted in accordance with the opinion of the Court, without prejudice to the respondent's right to contest the correctness of the decision entered herein by the Court, pursuant to the statutes in such cases made and provided.

/s/ CHARLES OLIPHANT,  
Chief Counsel, Bureau of  
Internal Revenue.

/s/ CHARLES OLIPHANT,   ECC.  
Of Counsel:

B. H. NEBLETT,  
Division Counsel.

E. C. CROUTER,  
Special Attorney, Bureau of  
Internal Revenue.

C-TS:PD  
LA:KD

Recomputation Statement  
In re: Birch Ranch and Oil Company  
427 West Fifth Street  
Los Angeles 13, California

Jan. 18, 1950.

Docket No. 8720

Tax Liability

Year Ended	Liability	Assessed Income Tax	Deficiency
9/30/41	\$7,833.44	None	\$7,833.44
9/30/42	None	None	None
	<u>\$7,833.44</u>	<u>None</u>	<u>\$7,833.44</u>
	Declared Value Excess Profits Tax		
9/30/41	\$4,565.41	None	\$4,565.41
9/30/42	None	None	None
	<u>\$4,565.41</u>	<u>None</u>	<u>\$4,565.41</u>

The attached schedules of tax computation were prepared under Rule 50 pursuant to the opinion of the Tax Court, promulgated December 15, 1949.

Birch Ranch and Oil Company      Recomputation Statement  
Taxable Year Ended Sept. 30, 1941

Schedule 1

Net income shown in the statutory notice of deficiency dated April 30, 1945 .....	\$34,711.24
Revised in accordance with the Tax Court's opinion (unchanged) .....	34,711.24
	Declared Value Excess Profits Tax
Tax liability (unchanged) .....	\$7,833.44
Tax assessed .....	None
Deficiency .....	\$7,833.44*      \$4,565.41*

\* Note: These taxes were paid 7-7-47 to the Collector of Internal Revenue, who is holding as a deposit in a 9-D suspense account.

Taxable Year Ended Sept. 30, 1942

Schedule 2

Adjustments to Net Income

Net income shown in the statutory notice of deficiency dated April 30, 1945 .....	\$ 37,781.08
Revised (net loss) .....	(64,769.60)
Difference (decrease) .....	<u>\$102,550.68</u>



## Schedule 3

## Explanation of Adjustment

Net operating loss deduction is allowed as the result of a carry-back from the taxable year ended September 30, 1944. For computation see Exhibit A, herewith.

## Schedule 4

## Computation of Tax

	Income Tax	Declared Value Excess Profits Tax
Revised net income (loss), schedule 1..	(\$64,769.60)	(\$64,769.60)
Tax liability .....	None	None
Tax assessed .....	None	None
Deficiency .....	None	None

## Exhibit A

Computation of Net Operating Loss Deduction  
Taxable Year Ended Sept. 30, 1946

Net income shown in the revenue agent's report (re-examination) dated 11-7-47 .....	None
Add: Operating loss deduction (1946 carry-back) reversed .....	\$ 34,711.50
Contributions limited under section 23(q) .....	1,010.00
Total .....	\$ 35,721.50
Less: Taxes held allowable in the Tax Court's opinion .....	221,610.87
Net loss carry-back .....	\$185,889.37
Less:	
Adjustment—Section 122 Internal Revenue Code:	
Section 122(b), percentage depletion year 1944 .....	\$42,372.60
Section 122(c):	
Percentage depletion 1942 .....	35,806.09
Interest on U.S. obligations .....	5,160.00
Net operating loss deduction .....	\$102,550.68

Received and Filed T.C.U.S. January 24, 1950.

The Tax Court of the United States  
Washington

Docket No. 8720

BIRCH RANCH & OIL COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

DECISION

This proceeding was called from the hearing calendar of March 1, 1950, for settlement pursuant to Rule 50. No appearance was made on behalf of the petitioner, and upon consideration of the respondent's computation filed on January 24, 1950, it is

Ordered and Decided: That there are deficiencies for the fiscal year ended September 30, 1941, in income tax and declared value excess-profits tax in the respective amounts of \$7,833.44 and \$4,565.41; and further, that there are no deficiencies in income tax and declared value excess-profits tax for the fiscal year ended September 30, 1942.

/s/ LUTHER A. JOHNSON,  
Judge.

Entered Mar. 3, 1950.

Served Mar. 6, 1950.

In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 8720

COMMISSIONER OF INTERNAL REVENUE,

Petitioner on Review,

vs.

BIRCH RANCH AND OIL COMPANY,

Respondent on Review.

PETITION FOR REVIEW AND  
STATEMENT OF POINTS

To the Honorable Judges of the United States  
Court of Appeals for the Ninth Circuit:

The Commissioner of Internal Revenue petitions The United States Court of Appeals for the Ninth Circuit to review the decision entered by The Tax Court of the United States on March 3, 1950, pursuant to its Findings of Fact and Opinion promulgated December 15, 1949, ordering and deciding "that there are deficiencies for the fiscal year ended September 30, 1941, in income tax and declared value excess-profits tax in the respective amounts of \$7,833.44 and \$4,565.41; and further, that there are no deficiencies in income tax and declared value excess-profits tax for the fiscal year ended September 30, 1942." This petition for review is filed pursuant to the provisions of Sections 1141 and 1142 of the United States Internal Revenue Code as amended.

## I.

## Jurisdiction

Birch Ranch and Oil Company, respondent on review herein, is a corporation organized under the laws of the State of Nevada on or about October 15, 1934, with its place of business at Los Angeles, California, and filed its Federal income and declared value excess-profits tax return for the fiscal year ended September 30, 1942, herein involved, with the Collector of Internal Revenue for the Sixth District of California located at Los Angeles, California, which collection district is within the jurisdiction of The United States Court of Appeals for the Ninth Circuit, wherein review is sought. This case involves Federal income and declared value excess-profits taxes for the fiscal year ended September 30, 1942.

## II.

## Nature of Controversy

The question to be presented to the reviewing court is: Is taxpayer entitled to a deduction in the taxable year 1944, resulting in a net operating loss carry-back to 1942 under Section 122(b)(1) of the Code, on account of payments made on call for so-called "interest or taxes" in the aggregate amount of \$221,610.87, including delinquency penalties, assessed on behalf of a California Reclamation District upon improvements to lands comprising such district all of which land was practically owned and operated by taxpayer, with which to pay the tax-exempt interest on the district's bonds, substantially



all of which were owned or controlled by taxpayer's sole stockholders?

The taxpayer-corporation, whose sole stockholders were A. Otis Birch and wife and whose books were kept on a cash basis, owned substantially all the land comprised in a California reclamation district, known as "Conaway Ranch," upon which its predecessor-partnership, the Birch Oil Company, owned by the "Birch family group" constructed and made drainage improvements at a cost of \$2,000,000. at the instigation and direction of the reclamation state board for which it received a warrant in payment. Thereafter \$2,000,000. of 6% district bonds were sold to Birch for which the warrant was given in payment and part of the bonds were distributed or sold to others. However, by the middle of 1944 Mr. and Mrs. Birch had acquired all of the bonds except 10 which were owned by Mr. Birch's cousin. The principal and interest were payable out of moneys collected by the county from assessments against benefited land and although the last of the bonds were to mature on January 1, 1943, no amount was ever paid into the district by the Birchs or the taxpayer for the purpose of paying them off. For all practical purposes the taxpayer and the district were one and the same. Calls for the so-called "taxes" were made at the taxpayer's and Birch's convenience and during the taxable year 1944 calls aggregating the sum of \$221,610.87, including delinquency penalties, were made for assessments against the "Conaway Ranch" for which to pay interest due and past due for prior years.

The aforementioned payments were deducted in 1944 as "taxes paid" and were disallowed by the Commissioner. Their allowance results in a "net carry-back loss" for the taxable year 1944 in the amount of \$185,889.37 and an adjusted net operating loss deduction of \$102,550.68 carry-back to 1942 (Section 122(b) of Internal Revenue Code), which eliminates the entire net income as adjusted for 1942 in the amount of \$37,781.08 and the proposed deficiencies in income and declared value excess profits taxes in the respective amounts of \$11,915.67 and \$1,687.10, exclusive of interest due thereon.

The Commissioner contended before the Tax Court that the claimed deduction for "interest or taxes" paid during 1944 were properly disallowed and accordingly there is no net operating loss carry-back to the year 1942, because (1) the reclamation district was a fiction, indistinguishable from the taxpayer-corporation and its stockholders; (2) the corporate identity of the taxpayer should be disregarded as far as any alleged liability to its stockholders are concerned; (3) there was a merger of all liens and estates and any liability for interest or taxes was extinguished and (4) the payments of "interest" on reclamation bonds during the taxable year constituted payments of indebtedness incurred and continued to purchase or carry obligations, the interest upon which is wholly exempt from Federal tax, which is not deductible under Section 23(b) of the Code; and further the payments were not ordinary and necessary expenses incurred or paid in

1944 in operating the ranch in such year but to pay interest to its stockholders on tax-exempt bonds.

In holding adversely to the Commissioner the Tax Court found that "as all of the \$221,610.87 paid to the county treasurer was for application to interest charges, none of it is excluded as a deduction by the statutory exceptions "under Section 23(c)(1)(E) of the Code. It also concluded that, although it may ignore the negligible 240 district acres which taxpayers did not own and against which no calls apparently were made, it could not ignore a "public district" invested with taxing powers and other sovereign attributes and the substance attaching to the number of bonds which were held by parties who had no identity of economic interest with the Birchs in respect to which deductions had been allowed and approved in prior year proceedings of this taxpayer (T.C. Docket No. 109993—3 T.C.M. 378—1944, *aff'd* CA-9, 1946, 152 F. (2) 874, *c.d.* 328 U.S. 863). Thus recognizing the districts as a legal entity, it viewed the taxpayer's "payments as made in satisfaction of taxes, and not of interest on indebtedness incurred and continued to purchase and carry tax-exempt obligations," and "as taxes assessed for interest only, they are not of a kind tending to increase the value of the property assessed, and hence are properly deductible."

The Commissioner presents that the record supports his position that since the taxpayer owned all the land of the district upon which calls were made and it or its stockholders owned substantially all the bonds of the district, the taxpayer's obligation to

pay "taxes" and the district's obligation to pay "interest" on the bonds was lacking in substance. Also that the district was in fact, if not in form, a private district; that in actual operation it was treated as a private district because no assessment taxes were paid from 1937 to 1943, no sinking fund was created, and the fiction of a public district was artificially kept alive to the end that taxpayer might deduct the amount which it paid as taxes, which amount it or its two stockholders received back as tax-exempt interest. The parties stipulated that the taxpayer and the district were one and the same for all practical operating purposes but the Tax Court apparently gave little weight to this part of the stipulation.

Even if there was a bona fide district originally organized, the agreed facts show that Mr. Birch and his wife acquired complete ownership and control of the district and ranch by 1944, except for 10 bonds, which were owned by Mr. Birch's cousin. The other bonds owned in prior years and the early part of 1944 were either owned by members of the "Birch family group"—cousins and nieces—and by a corporation of which Birch was president and a director. Mr. Birch and his wife merely used this device to siphon off large ranching profits from 21,000 acres in the guise of payment of "taxes" to the county treasurer, who would then repay similar amounts to Birch and his wife as tax-exempt interest. These payments were made largely to suit the convenience of the Birch's and the taxpayer, which kept its books and filed its returns on a cash basis.



The bonds began to mature on January 1, 1935, and were to be retired by January 1, 1943, and as of the time of the hearing herein on June 30, 1947, no amount had been ever assessed by or paid to the county or the district by either the Birchs or the taxpayer for the purpose of paying off the bonds. The resulting effect of the arrangement in 1944 and thereafter, as sustained by the decision of the Tax Court, establishes a continuing tax-avoidance loophole whereby taxpayers deduct payments for so-called taxes when it decides to call for them to pay its shareholders tax-exempt interest at six per cent on the bonds. Such a resulting tax avoidance scheme is contrary to the principles of *Higgins v. Smith* (1940) 308 U.S. 473 and *Gregory v. Helvering* (1935) 293 U.S. 465.

If such payments are deductible, then it is further presented that, in the alternate, in allowing a deduction for "penalties" as part of the aggregate payment made of \$221,610.87—contrary to *Helen B. Achelis* (1933) 28 B.T.A. 244, 246 and cases cited and *Edward G. Acheson Jr.*, T.C. Memo. Op. (1943) 1 T.C.M. 877—the Tax Court also erred.

### III.

#### Statement of Points

That the Commissioner of Internal Revenue, being aggrieved by the opinion and decision of The Tax Court of the United States in this proceeding, hereby petitions for a review of said opinion and decision by The United States Court of Appeals for the Ninth Circuit, and for the correction of the

manifest errors which therein occurred and intervened to his prejudice. The Commissioner submits the following statement of points upon which he intends to rely as the basis of this petition for review:

That the Tax Court of the United States erred:

1. In holding and deciding that under the circumstances involved herein, the amounts paid on call of the county treasurer as "taxes" to meet interest on bonds of a California reclamation district are deductible in the taxable year 1944 under Section 23 of the Internal Revenue Code.

2. In failing to hold and decide that under the circumstances involved herein, the amounts paid on call of the county treasurer as "taxes" to meet interest on bonds of a California reclamation district are not deductible in the taxable year 1944 under Section 23 of the Internal Revenue Code.

3. In holding and deciding that the taxpayer is entitled to a deduction for "taxes to meet interest" in the taxable year 1944 in the amount of \$221,610.87.

4. In failing to hold and decide that taxpayer is not entitled to any deduction for "taxes to meet interest" in the taxable year 1944.

5. In holding and deciding that taxpayer's assessment payments used to pay interest on the bonds in the taxable year 1944 are deductible under and because of its prior decision covering the years 1937 and 1939 of this taxpayer in Docket No. 109993—

(3 T.C.M. 378—1944, aff'd CA-9, 1946, 152 F. (2) 874, c.d. 328 U.S. 863).

6. In holding and concluding that all of the \$221,610.87 paid to the county treasurer was “for application to interest charges” and accordingly none of it is excluded as a deduction by the statutory exceptions under the provisions of subparagraph E of Section 23(c) of the Internal Revenue Code.

7. In holding and finding that the payments of \$221,610.87 were made in satisfaction of “taxes” and not “interest” and were not of a kind tending to increase the value of the property assessed within the meaning of Subsection (a) of Section 23(c)(1) of the Internal Revenue Code.

8. In failing to hold and decide that the “payments of interest on reclamation bonds” were the payment of interest on indebtedness incurred and continued to purchase and carry tax-exempt obligations and hence not deductible under Section 23(b) of the Internal Revenue Code.

9. In failing to hold and find that the tax and interest payments had no business purpose and did not discharge any real legal obligation.

10. In holding and deciding that the Reclamation District No. 2035 was a “public district” and operated as such.

11. In failing to hold and find that taxpayer's obligation to pay taxes and the district's obligation

to pay interest on the bonds, under the circumstances, was lacking in substance.

12. In holding and deciding that since the Reclamation District was a "public district" or legal entity it could not be disregarded under the circumstances involved herein.

13. In failing to hold and find that the Reclamation District No. 2035 was in fact, if not in form, a private district and operated as such.

14. In failing to hold and find that the Reclamation District No. 2035 was in reality a mere fiction indistinguishable from the taxpayer and its sole stockholders.

15. In holding and finding that a very large number of bonds were held by parties who had no identity of economic interest with Mr. and Mrs. Birch.

16. In failing to hold and find that the Birchs, the taxpayer and the reclamation district were all one and the same in substance.

17. In failing to hold and find that when Mr. Birch and his wife re-acquired the bonds all prior lien and taxes were merged and extinguished.

18. In holding and deciding that taxpayer is entitled to a net operating loss carry-back deduction for the taxable year 1944 available for the taxable year 1942 in the amount of \$102,550.68 under Section 122(b) of the Internal Revenue Code.

19. In failing to hold and decide that there was



no net loss carry-back for the taxable year 1944 available as a deduction for the taxable year 1942 under Section 122(b) of the Internal Revenue Code.

20. In failing to hold and decide that taxpayer realized a net taxable income in the amount of \$35,721.50 for the taxable year 1944.

21. In failing to hold and decide, in the alternate, that the 10 per cent added to the assessment for taxes and paid on account of delay in payment of such taxes, is a penalty and nondeductible for Federal income tax purposes.

22. In failing to hold and decide, in the alternate, that such portion of the aggregate payment of \$221,610.87 that constitute "delinquent penalties" are not deductible as taxes.

23. In that its opinion and decision are contrary to the law and the regulations and is not supported by substantial evidence of record.

24. In ordering and deciding that there are no deficiencies in income tax and declared value excess profits tax for the fiscal year ended September 30, 1942.

25. In failing to order and decide that there are deficiencies in income tax and declared value excess profits tax for the fiscal year ended September 30, 1942, in the respective amounts of \$11,915.67 and \$1,687.10.

Wherefore, the Commissioner petitions that said findings of fact and opinion and decision of The

Tax Court of the United States be reviewed by The United States Court of Appeals for the Ninth Circuit; that a transcript of the record be prepared in accordance with the law and the rules of said Court and be transmitted to the Clerk of the said Court for filing; and that appropriate action be taken to the end that the errors herein complained of may be reviewed and corrected by said Court.

/s/ THERON L. CAUDLE, CAR  
Assistant Attorney General.

/s/ CHARLES OLIPHANT, CAR  
Chief Counsel Bureau of Internal Revenue  
Counsel for Petitioner on Review.

Of Counsel:

CLAUDE R. MARSHALL,  
Special Attorney  
Bureau of Internal Revenue.

Received and Filed T.C.U.S. May 19, 1950.

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[Title of Court of Appeals and Cause.]

NOTICE OF FILING PETITION  
FOR REVIEW

To: George Acret, Esq.,  
650 South Grand Avenue  
Los Angeles 14, California

You are hereby notified that the Commissioner of Internal Revenue did, on the 19th day of May, 1950,

file with the Clerk of The Tax Court of the United States, at Washington, D. C., a petition for review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court heretofore rendered in the above-entitled cause. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 19th day of May, 1950.

/s/ CHARLES OLIPHANT, CAR  
Chief Counsel, Bureau of Internal Revenue  
Counsel for Petitioner on Review.

Service acknowledged.

Received and Filed T.C.U.S. May 31, 1950.

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[Title of Court of Appeals and Cause.]

NOTICE OF FILING PETITION  
FOR REVIEW

To: R. R. Landrum, Secretary  
Birch Ranch & Oil Company  
427 West Fifth Street  
Los Angeles, California

You are hereby notified that the Commissioner of Internal Revenue did, on the 19th day of May, 1950, file with the Clerk of The Tax Court of the United States, at Washington, D. C., a petition for review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court heretofore rendered in the above-entitled cause. A

copy of the petition for review as filed is hereto attached and served upon you.

Dated this 19th day of May, 1950.

/s/ CHARLES OLIPHANT, CAR  
Chief Counsel, Bureau of Internal Revenue  
Counsel for Petitioner on Review.

Service acknowledged.

Received and Filed T.C.U.S. May 31, 1950.

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[Title of Court of Appeals and Cause.]

### MOTION

Now Comes the Commissioner of Internal Revenue, petitioner on review in the above-entitled cause, by and through his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and moves that the time within which to prepare, transmit and deliver the record on review in this cause in The United States Court of Appeals for the Ninth Circuit be extended to and including August 17, 1950, and for cause shows:

That a petition to have the Tax Court's decision herein reviewed by the Court of Appeals for the Ninth Circuit was filed on May 19, 1950; that the time for filing the record on review now expires on June 28, 1950; that the matter of the disposition of this cause is still under consideration by the Government and that the determination of such further action will be made within the next 45 days; that



the preparation and transmittal of the transcript of record on review under the above circumstances would require unnecessary expenses to the parties herein; and that in any event the record herein cannot be completed and filed within the time now allowed.

Wherefore, it is prayed that this motion be granted.

/s/ CHARLES OLIPHANT,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

CLAUDE R. MARSHALL,

Special Attorney,

Bureau of Internal Revenue.

Received and Filed T.C.U.S. June 19, 1950.

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The Tax Court of the United States  
Washington

Docket No. 8720

COMMISSIONER OF INTERNAL REVENUE,  
Petitioner,

vs.

BIRCH RANCH & OIL COMPANY,  
Respondent.

ORDER ENLARGING TIME

Upon motion of counsel for petitioner, it is  
Ordered that the time for preparation, transmis-

sion and delivery of the record sur petition for review of the above-entitled proceeding in the United States Court of Appeals for the Ninth Circuit is extended to August 17, 1950.

[Seal]      /s/ J. E. MURDOCK,  
Acting Presiding Judge.

Dated: Washington, D. C., June 19, 1950.

Served June 21, 1950.

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In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 8720

COMMISSIONER OF INTERNAL REVENUE,  
Petitioner on Review,

vs.

BIRCH RANCH AND OIL COMPANY,  
Respondent on Review.

### NOTICE OF RECORD ON REVIEW

To the Clerk of The Tax Court of the  
United States:

Pursuant to the provisions of rule 11 of the amended rules of The United States Court of Appeals for the Ninth Circuit, you are hereby notified that the petitioner on review will not exclude or omit any of the original papers made a part of the

record in this proceeding before The Tax Court of the United States.

/s/ THERON L. CAUDLE,  
Assistant Attorney General.

/s/ CHARLES OLIPHANT,  
Chief Counsel, Bureau of Internal Revenue  
Counsel for Commissioner of Internal Revenue.

Consented to:

/s/ GEORGE ACRET,

Received and Filed July 6, 1950.

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The Tax Court of the United States  
Washington

[Title of Cause.]

### CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents, 1 to 52, inclusive, constitute and are all of the papers and proceedings on file in my office as the original and complete record in the proceeding before The Tax Court of the United States entitled: "Birch Ranch and Oil Company, Petitioner, v. Commissioner of Internal Revenue, Respondent," Docket No. 8720 and in which the respondent in the Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said

Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 1st day of August, 1950.

[Seal]        /s/ VICTOR S. MERSCH,  
                 Clerk.

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[Endorsed]: No. 12639. United States Court of Appeals for the Ninth Circuit. Commissioner of Internal Revenue, Petitioner, vs. Birch Ranch and Oil Company, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed August 7, 1950.

                 /s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.



In the United States Court of Appeals  
for the Ninth Circuit

No. 12,639

COMMISSIONER OF INTERNAL REVENUE,  
Petitioner,

vs.

BIRCH RANCH & OIL CO.,

Respondent.

PETITIONER'S DESIGNATION OF CON-  
TENTS OF PRINTED RECORD ON REVIEW

The petitioner, by and through his undersigned attorney, pursuant to the provisions of Rule 19(6) of this Court, hereby designates the entire record of the proceedings in the above-styled cause to be printed on review, with the exception of Petitioner's Exhibits 1 through 12, inclusive, 14 and 15, Respondent's Exhibits B through E, inclusive, and Joint Exhibits 3a and 13f, which counsel for the respective parties hereto have stipulated may be physically transmitted to the Court.

Dated this 15th day of August, 1950.

/s/ THERON LAMAR CAUDLE,  
Assistant Attorney General,  
Counsel for the Petitioner.

Receipt of the above and foregoing Petitioner's Designation of Contents of Printed Record on Review is acknowledged this 18th day of August, 1950.

/s/ GEORGE ACRET,  
Counsel for the Respondent.

[Endorsed]: Filed August 21, 1950.

[Title of Court of Appeals and Cause.]

STIPULATION AND ORDER

It is hereby stipulated by and between counsel for the respective parties hereto, subject to the approval of the Court, that Petitioner's Exhibits 1 through 12, inclusive, 14 and 15, Respondent's Exhibits B through E, inclusive, and Joint Exhibits 3a and 13f shall not be required to be printed as part of the record herein, but may be physically transmitted to the Court; counsel for both parties reserving the right to refer to the aforementioned exhibits on brief or in argument in all respects as if they constituted part of the printed record, however.

Dated this 15th day of August, 1950.

/s/ THERON LAMAR CAUDLE,  
Assistant Attorney General,  
Counsel for Petitioner.

/s/ GEORGE ACRET,  
Counsel for Respondent.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ CLIFTON MATHEWS,

/s/ WM. E. ORR,  
United States Circuit Judges.

[Endorsed]: Filed August 22, 1950.



No. 12639

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**In the United States Court of Appeals  
for the Ninth Circuit**

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COMMISSIONER OF INTERNAL REVENUE, PETITIONER

*v.*

BIRCH RANCH AND OIL COMPANY, RESPONDENT

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ON PETITION FOR REVIEW OF THE DECISION OF THE TAX  
COURT OF THE UNITED STATES

---

**BRIEF FOR THE PETITIONER**

---

THERON LAMAR CAUDLE,  
*Assistant Attorney General.*

ELLIS N. SLACK,  
A. F. PRESCOTT,  
MELVA M. GRANEY,

*Special Assistants to the Attorney General.*

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**FILED**

NOV 20 1950

PAUL P. O'BRIEN,  
CLERK





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**In the United States Court of Appeals  
for the Ninth Circuit**

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No. 12639

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

*v.*

BIRCH RANCH AND OIL COMPANY, RESPONDENT

---

*ON PETITION FOR REVIEW OF THE DECISION OF THE TAX  
COURT OF THE UNITED STATES*

---

**BRIEF FOR THE PETITIONER**

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**OPINION BELOW**

The findings of fact and opinion of the Tax Court (R. 385-408) are reported at 13 T.C. 930.

**JURISDICTION**

The Commissioner determined deficiencies in income and declared value excess profits taxes for the fiscal years ended September 30, 1941 and 1942, and mailed notice of the deficiencies to taxpayer on April 30, 1945. (R. 25-26.) On July 13, 1945, within the permitted 90-day period, taxpayer filed a petition for review with the Tax Court for a redetermination of the deficiencies under the provisions of Section 272 of the Internal Revenue Code. (R. 1, 5-25.) Taxpayer subsequently

filed an amended petition (R. 33-52) which, among other things, raised an issue as to its right to a carry-back deduction to the year 1942 for a net operating loss sustained in 1944 (see R. 51). The Commissioner filed an answer to the amended petition (R. 53-55) and, after a brief hearing on June 30, 1947 (R. 56-99), the Tax Court, in a memorandum opinion (R. 100-115), held that it had jurisdiction of the carry-back deduction issue. *Birch Ranch & Oil Co. v. Commissioner*, decided March 24, 1948 (1948 P-H T.C. Memorandum Decisions, par. 48,040). A further hearing was held October 11, 1948. (R. 117.) Taxpayer abandoned issues other than the carry-back deduction issue (R. 387) and filed a supplement and amendment to the petition relating to the carry-back deduction issue (R. 127-131). The Commissioner filed an answer (R. 131-133) and further hearing in the case was had on February 15, 1949 (R. 149). The decision of the Tax Court was entered March 3, 1950. (R. 411.) The Commissioner's petition for review by this Court (R. 412-423) was filed May 19, 1950 (R. 4, 423-424), and properly invoked the jurisdiction of this Court under Section 1141(a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948.

#### QUESTION PRESENTED

Whether the circumstances of the case are such as to entitle the taxpayer-corporation to a "taxes paid" deduction under Section 23 (c) of the Internal Revenue Code, or to an "interest paid" deduction under Sections 23 (b), 122 (a) and (d) (2), in computing its 1944 net operating loss for the purpose of a carry-back deduction in the taxable year 1942 under Sections 23 (s) and 122.

#### STATUTE AND REGULATIONS INVOLVED

The pertinent statute and Treasury Regulations are set forth in the Appendix, *infra*.

## STATEMENT

The Tax Court's findings of fact (R. 387-397) are as follows:

Taxpayer is a Nevada corporation having its principal office at Los Angeles, California. It was organized on October 15, 1934, by A. Otis Birch and his wife, M. Estelle C. Birch, who on the same date also organized the Birch Securities Company and the Birch Holding Company. To the taxpayer-corporation Birch and his wife transferred a 21,000-acre tract of land known as the Conaway Ranch and certain other property. To the Birch Securities Company Birch and his wife transferred 1,594 bonds, each of \$1,000 face value, issued by Reclamation District No. 2035 (California), certain stocks, and other assets. The two transfers comprised all of their property. All shares of the taxpayer-corporation and of the Birch Securities Company were transferred to the Birch Holding Company, which issued 49 per cent of its shares to Birch and 51 per cent to Birch's wife. (R. 387-388.)

Birch was president and in control of the affairs of all three corporations. The Birch Securities Company and the Birch Holding Company were formed for convenience and conducted no business. The taxpayer-corporation operated the Conaway Ranch, raising and selling crops and sheep. (R. 388.)

The Conaway Ranch is situated in Yolo County, California, about five miles from Sacramento. It was purchased in 1914 and thereafter enlarged by the Birch Oil Company, a partnership in which Birch and his wife, the wife's parents, and Birch's nieces (hereinafter called the Hopkins sisters) held interests. (R. 388.)

At the time of the initial purchase, the Sacramento and San Joaquin Drainage District, created under the laws of California, was making surveys in the area for a



flood control project, and the reclamation board of the state later informed the Birch Oil Company that if it would construct a levee across the ranch adjacent to a proposed Yolo bypass, an assessment would be made against all lands in the drainage district to pay for the construction and for flowage rights. Desiring to develop its land, the Birch Oil Company later petitioned the supervisors of Yolo County to create a reclamation district which would comprise the ranch, and in April, 1919, the supervisors approved the establishment of Reclamation District No. 2035. B. F. Conaway, Birch's father-in-law, C. Harold Hopkins, the husband of Birch's niece, and a local attorney were appointed District trustees. A program of improvements, estimated to cost \$2,264,740, was authorized, and commissioners were named who apportioned the cost of the improvements among lands in the District according to the benefits to be received, and filed with the treasurer of Yolo County assessments against the lands to meet such cost. (R. 388-389.)

The Birch Oil Company, under direction of the District's engineer, constructed the improvements, which consisted of many miles of roadways, canals, ditches, bridges, pumping plants, and other structures, at a cost of slightly over \$2,000,000. It financed the work, and after completion in 1924 received a warrant, dated January 5, 1925, directing that the District, through the treasurer of Yolo County, pay it \$2,000,000. (R. 389.)

On January 23, 1925, 2,000 bonds of the District, each of a par value of \$1,000, were offered at auction to provide the necessary funds, and Birch purchased all of them, giving the \$2,000,000 warrant in payment. These bonds bore six per cent interest, payable on January 1 and July 1 of 1925 and each year thereafter on presentation of an interest coupon to the county treasurer; 227 bonds were to mature on January 1 of 1935 and a like

number on January 1 of each succeeding year, ending with maturity of the last 184 on January 1, 1943. Principal and interest were payable out of moneys collected by the treasurer of Yolo County from assessments against the benefited lands, which assessments were to be deposited "into the main county treasury", but "credited to the bond fund" of the District, as provided by Section 3480, Article II, c. 1, Title 8, Deering's Political Code of California. (R. 389-390.)

Pursuant to a contract of 1924 Birch and his wife purchased the Hopkins sisters' interest in the ranch and Birch Oil Company, and in 1926 they purchased the wife's parents' interest. By virtue of these acquisitions and the purchase of small adjacent parcels of land they came into ownership of the entire ranch, then consisting of about 21,000 acres. The ranch was coterminous with Reclamation District No. 2035, except for 1,300 ranch acres which lay outside the District and 240 District acres which lay outside the ranch. (R. 390.)

In buying the interests of the Hopkins sisters, Birch paid them \$1,000 cash and 786 District bonds.<sup>1</sup>

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<sup>1</sup> In this connection the stipulation of facts states (R. 138-139, 140):

9. In the meantime, the Hopkins sisters, being desirous of disposing of their interests in the Conaway Ranch, by agreements dated January 1, 1924, sold such interests to Birch and Mrs. Birch for \$787,000, an amount designed to pay them their proportionate part of the Birch Oil Company funds invested in the ranch. Under the agreements each of the sisters agreed to accept bonds of Reclamation District No. 2035 in the principal amount of \$393,000 and cash in the sum of \$500. Birch and his wife agreed to cause the district to issue bonds in an amount of at least \$800,000, which were to constitute a prior lien on all of the property in the district, and further promised to deliver on or before February 1, 1925, to each of the sisters the amount of the bonds and cash called for by the agreements. Birch and his wife were to have immediate and absolute possession and control of the properties acquired from the Hopkins sisters and were to be entitled to all rents and profits of every

Simultaneously, he and his wife agreed to buy back from them the 786 bonds at face value in specified annual installments on January 1 of each year from 1926 to 1934, and as security for performance they placed their remaining 1,214 bonds with trustees empowered to sell and make good any default by them on the contract. The Hopkins sisters, however, reserved the right not to sell on any installment date. During the first six years Birch and his wife paid for and received 476 bonds, as contemplated by the contract.

Because of financial difficulties they thereafter ceased to purchase installments of the remaining 310. But instead of invoking action by the trustees, the Hopkins sisters granted them a time extension without release from the obligation to buy. Prior to 1937 Birch and his wife sold ten of their District bonds to Lula Minter, a cousin of Birch, and 86 to the Great Republic Life Insurance Company, of which Birch was president and a director. (R. 390-391.)

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kind therefrom and were to assume all liabilities and burdens incident to the ownership thereof. The bonds not having been issued at the time of the agreements on January 1, 1924, Birch gave to each of the sisters his promissory note in an amount equal to the amount of the bonds she was entitled to receive under the agreements. The notes were to run for 10 years and were to draw interest at 6 per cent per annum from January 1, 1924, for a period of 5 years, and at 7 per cent thereafter. Birch had the option of paying the notes in full at any time prior to the expiration of the 10 year period.

\* \* \* \* \*

13. Upon receipt of the bonds of the district, Birch delivered to each of the Hopkins sisters \$393,000 par value of such bonds, or a total of \$786,000 pursuant to the agreements of January 1, 1924, whereunder he and his wife had acquired from the Hopkins sisters all of the interests of the latter in the Conaway Ranch. Upon delivery of the bonds, the Hopkins sisters delivered to Birch the promissory notes covering the purchase price of their interests in the ranch which had been received from him at the time of the January 1, 1924 agreements. At the same time they made formal conveyance to Birch and his wife of all their interests in the Conaway Ranch.



During the years 1925-1930 Birch and his wife paid to the county treasurer of Yolo County on call of the assessment against the ranch the amounts necessary to meet interest payments on the bonds, and the Hopkins sisters collected their interest from the treasurer on presentation of the matured coupons. In succeeding years Birch bought the coupons of the Hopkins sisters as they matured, and deposited them with the treasurer, receiving a receipt and credit on the assessment against the ranch. After the taxpayer-corporation acquired the ranch in 1934, it too purchased at face value matured interest coupons from the Hopkins sister and from Lula Minter, turning them in to the county treasurer. It did not buy matured coupons on the 86 bonds held by the insurance company, and that company's successor in interest eventually brought suit to enforce collection of interest. The suit was settled by the taxpayer-corporation's purchase of the 86 bonds and accrued interest in 1940 for \$65,000. (R. 391-392.)

No amount was ever paid into the Reclamation District by Birch and his wife or by the taxpayer-corporation for the purpose of paying off the bonds. But prior to maturity of the first 227 bonds and in 1935 the original issue was refunded by 2,000 new six per cent bonds of \$1,000 face value, of which 50 were to mature on January 1 of 1945 and of each succeeding year. (R. 392.)

To test the legality of the original issue the District trustees filed a complaint with the Superior Court of Yolo County, and after consideration of the evidence the court on March 2, 1925, entered a decree that "said bonds are a valid, legal obligation of said Reclamation District No. 2035 \* \* \*". The refunding bonds were likewise held a legal obligation of the District by decree entered in a similar proceeding on June 25, 1935. The proceedings were not contested. (R. 392.)



Since its organization in 1934 the taxpayer-corporation has operated the Conaway Ranch and has borne all costs and expenses of maintaining and operating the improvements of the Reclamation District, treating such disbursements as part of its expenses in operating the ranch in a manner which would be no different if there were no reclamation District, whether formal or actual, and the District has no expenses which are not taken care of by the taxpayer-corporation. For its ranch operations the taxpayer-corporation keeps a set of books on the basis of cash receipts and disbursements. (R. 392.)

The officials of California counties are lenient with the owners of assessed lands in reclamation districts, and, while there was no express agreement, the treasurer of Yolo County refrained, in and after 1937, from making any calls on the taxpayer-corporation for payments or declaring defaults or taking foreclosure action against the ranch, being aware that the taxpayer-corporation was in no position to pay an assessment. The taxpayer-corporation nonetheless accrued on its books and deducted on its income tax returns an amount of \$120,000 a year for which a call could have been made to provide the county treasurer with moneys necessary for the payment of the annual six per cent interest on the \$2,000,000 face value bonds. It continued to buy at face value the maturing interest coupons on the 310 bonds of the Hopkins sisters and the ten bonds of Lula Minter, paying \$18,600 and \$600 a year, respectively, for them. (R. 393.)

The Commissioner allowed a deduction of the \$600 plan to Lula Minter, but disallowed the rest of the \$120,000 claimed. The taxpayer-corporation contested such disallowances for 1937 and 1939 in a proceeding before the Tax Court, Docket No. 109993. The Tax Court held that the \$18,600 paid to the Hopkins sisters

was deductible, and sustained disallowance of the rest. *Birch Ranch and Oil Co. v. Commissioner*, decided April 20, 1944 (1944 P-H T. C. Memorandum Decisions, par. 44,128), affirmed January 6, 1946, 152 F. 2d 874 (C. A. 9th). This decision was based on a finding that the taxpayer-corporation kept its books for ranching operations on a cash, not on an accrual basis, and had made no payments other than the \$600 and the \$18,600. (R. 393.)

On September 30, 1943, the taxpayer-corporation held the 86 bonds acquired from the life insurance company; the Birch Securities Company held the 1,594 transferred to it at organization; the Hopkins sisters held 310 subject to the sale contract with Birch and his wife; and Lula Minter held 10. (R. 394.)

On March 15, 1944, Birch and his wife bought the remaining 310 bonds from the Hopkins sisters and the Birch Securities Company was liquidated and dissolved before the close of the fiscal year on September 30. The Birch Securities Company had been suspended since 1938 for failure to pay a state tax. (R. 394.)

Thus at the close of the fiscal year 1944 Birch and wife held directly 310 of the 2,000 bonds of the District; the Birch Holding Company held 1,594 from the liquidation of the Birch Securities Company; the taxpayer-corporation held 86; and Lula Minter 10. (R. 394.)

In March, 1943, the taxpayer-corporation and Birch and his wife gave to several individuals a written option to purchase the Conaway Ranch and all the District bonds. (R. 394.)

During the period 1937 until late in 1943 the taxpayer-corporation made no cash payment to the county treasurer to provide interest on the bonds and received no call to make a payment. In 1943, however, funds became available to it, and on October 13, 1943, the

treasurer made a call for \$58,565.92, payable November 12. The taxpayer-corporation advised the treasurer that it could not pay the amount until later and would submit to a delinquency penalty. In reply the treasurer explained that the penalty was "part and parcel of the Call" which was "for interest only". On December 28, 1943, the Birch Securities Company transmitted to the treasurer coupons from 166 bonds and advised that the trustees for the Hopkins sisters would present coupons from 1,278 bonds. It requested remittance of \$49,320 to cover the accrued interest. The following day the taxpayer-corporation paid the assessment call and a penalty of \$5,856.59 by its check for \$64,422.51 drawn in favor of the county treasurer, and the treasurer remitted \$49,320 interest to the Birch Securities Company on January 8, 1944. On April 10, 1944, the treasurer made another call, for \$53,721.65, payable May 10. The taxpayer-corporation paid this call and a ten per cent delinquency penalty of \$5,371.94 by its check for \$59,093.59 dated June 28, 1944. On August 12, 1944, the taxpayer-corporation gave to the treasurer its check for \$37,325.28 in satisfaction of the unpaid portion of a call dated December 1, 1935, together with penalty. Before making this remittance the taxpayer-corporation inquired of the treasurer by letter if the treasurer would pay the interest coupons in arrears upon receipt of the amount. On September 20, 1944, it paid the treasurer \$60,769.49 in satisfaction of a call dated September 8, 1944. In making calls, the treasurer computed an amount which, with any balance on hand, was sufficient to provide \$60,000 for the semiannual interest due on the bonds, and amounts paid as penalties were reflected in his computations. The four payments which the taxpayer-corporation made during its fiscal year 1944 aggregated \$221,610.87. Soon after the col-



lection of money by call the treasurer paid interest on the bonds, but no interest was ever paid without such preceding collection. (R. 394-395.)

On its tax returns for the fiscal years ended September 30, 1941, and 1942, the taxpayer-corporation claimed a deduction of \$120,000 on account of the tax due Reclamation District No. 2035, and for each year the Commissioner disallowed the deduction "except as to \$19,200 paid to the Hopkins sisters and Miss Minter". On July 7, 1947, after affirmance of the Tax Court's decision in Docket No. 109993, the taxpayer-corporation paid to the Collector \$12,398.85 on account of the deficiencies determined in its income and declared value excess profits taxes for the fiscal year 1941. As there had been no assessment of the determined deficiencies, the payment was credited by the Collector to a suspense account and not applied in satisfaction of a tax. (R. 395-396.)

On its return for the fiscal year ended September 30, 1944, the taxpayer-corporation claimed a deduction of \$118,890.87 as taxes paid to Reclamation District No. 2035, and reported a net loss of \$84,179.37 for the year. In a report dated January 23, 1947, addressed to the taxpayer-corporation, the revenue agent in charge of the Los Angeles division recomputed a net loss of \$186,899.37 for the year, and, in so doing, allowed a deduction of \$221,610.87, or the amount actually paid to the treasurer of Yolo County on account of the District taxes and penalties. (R. 396.) In a subsequent report, dated December 8, 1947, deduction of the \$221,610.87 was disallowed on the ground that (R. 396-397)—

there was no real or actual obligation outstanding against the taxpayer, since Reclamation District No. 2035 was comprised exclusively of the taxpayer's property, and since A. Otis Birch and his wife, Estelle Birch, the sole stockholders of the Birch



Ranch and Oil Company hold substantially all the bonds of the Reclamation District.

\* \* \* \* \*

As the interest received by A. Otis Birch and his wife, Estelle Birch, is nontaxable, the amounts claimed as taxes paid by the Birch Ranch and Oil Company is considered non-deductible.

As a consequence of this disallowance, the Commissioner determined that the taxpayer-corporation had no net loss carry-back from the fiscal year 1944 to the fiscal year 1942. (R. 397.)

On the basis of these facts, the Tax Court held that the taxpayer-corporation is entitled under Section 23 (c) of the Internal Revenue Code to a "taxes paid" deduction for the \$221,610.87 it paid to the county treasurer in 1944 and, accordingly, that the taxpayer-corporation had a net operating loss for 1944 which it may carry back and deduct in 1942. (R. 399-408.)

#### STATEMENT OF POINTS TO BE URGED

The Commissioner's statement of points is contained in the record at pages 418-423. Briefly, the Commissioner contends that the Tax Court erred in holding that taxpayer's aggregate \$221,610.87 payment in the fiscal year 1944 on "calls" by the county treasurer is deductible as "taxes". It is the Commissioner's position that the payment was and in any event should be treated as interest paid, rather than as taxes paid, and, except for the part of the payment received by the Hopkins sisters and Lulu Minter, is not deductible as interest paid.

#### SUMMARY OF ARGUMENT

Whether taxpayer is entitled to a net operating loss deduction for 1942 depends upon whether it had a net operating loss for 1944 to carry back to and deduct in 1942. Whether taxpayer had a net operating loss for

1944 depends upon whether it was entitled in 1944 to a deduction for the aggregate of \$221,610.87 it paid on "calls" made by the county treasurer to pay interest on bonds issued by Reclamation District No. 2035.

1. The Tax Court erred in holding that the payment is deductible under Section 23 (c) (1) (E) of the Internal Revenue Code as "taxes paid". In order to be deductible under that section the payment must have been of taxes assessed against public benefits and allocable to interest charges. It was allocable to interest charges but it was not of taxes assessed against local benefits. Such taxes are assessments levied against a property owner as compensation for the benefits received or, in other words, to pay the cost of the improvements. Here the improvements involved were paid for at the outset by the only party against whom taxes could otherwise have been levied to pay for the improvements. The "calls" by the county treasurer therefore were not "calls" for an enforced contribution toward the cost of the improvements, either principal or interest, and were not for payment of "taxes". The whole arrangement, although authorized by the law of California, was merely one through which the Birches had Reclamation District bonds issued for their own purposes and which they used to create personal indebtednesses. This is true even though the Reclamation District is considered a separate entity, for the existence of the Reclamation District cannot change the purpose of taxpayer's payments.

2. The \$221,610.87 was simply a payment of interest and, under the circumstances of this case, is not deductible as interest except for the part paid to the Hopkins sisters and Lulu Minter.

Section 23 (b) allows a deduction for interest paid "on indebtedness". Here there was no real indebted-

ness for interest other than on the bonds held by the Hopkins sisters and Lulu Minter. The payment of interest was made by the taxpayer-corporation, wholly owned by the Birches, and, except for the part received by the Hopkins sisters and Lulu Minter, was received by the Birches and their other two wholly-owned corporations, the Birch Securities Company and the Birch Holding Company. The payor and payees on those bonds were economically identical and no deduction for interest is allowable in such a case.

Moreover, Section 23(b) provides that no deduction for interest paid is allowable as to interest paid on indebtedness incurred to carry tax-exempt securities. For the purpose of computing net operating loss, such interest is the subject of a specific exception, addition or limitation. Section 122 (d)(2) provides that the tax-exempt interest shall be included in gross income and the interest paid to carry the tax-exempt securities is deductible against such included tax-exempt interest. According to the legislative reports, this exception was inserted for the purpose of insuring that only *economic* losses would be taken into account in computing net operating loss for carry-back purposes.

The interest received on the Reclamation District Bonds was tax-exempt. The interest paid on such bonds was interest paid to carry tax-exempt securities. Since the interest was paid by the taxpayer-corporation, a wholly-owned corporation of the Birches, and was received by the Birches and their other two wholly-owned corporations (except that received by the Hopkins sisters and Lulu Minter), no economic loss was involved. The separate entities of the wholly-owned corporations must be ignored in order to effectuate the Congressional intent, and, accordingly, the deduction for payment of interest, having been paid to carry tax-exempt securities, is not deductible.

3. Since Congress intended by Section 122 (d) (2) to insure that only economic losses would be taken into account in computing net operating loss, that purpose should not be thwarted by a holding that taxpayer's payments were of "taxes" and thus not subject to the limitations of Section 122 (d) (2). The Congressional purpose as to interest paid to carry tax-exempt securities is so clear as to require application even if taxpayer's interest payments may be considered interest paid through the medium of taxes. This is especially true when the payments were not of "taxes" in the usual sense of that word.

#### ARGUMENT

#### **Taxpayer Had No Net Operating Loss for 1944 to Carry Back to and Take as a Deduction in the Taxable Year 1942 under Sections 23 (s) and 122 of the Internal Revenue Code**

Section 23 (s) of the Internal Revenue Code (Appendix, *infra*) allows as a deduction "the net operating loss deduction computed under section 122". Under Section 122 the net operating loss deduction for a taxable year consists of such net operating losses of other years as may be carried over or carried back to the taxable year. In the present case the taxpayer-corporation is claiming that it had a net operating loss for 1944 which it may carry back to and take as a deduction in the taxable year 1942.<sup>2</sup> There is no dispute as to the right to carry back a 1944 net operating loss to 1942; the inquiry is whether taxpayer had a 1944 net operating loss to carry back. Section 122 (a) of the Code (Appendix, *infra*) provides that—

the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions, and limitations provided in subsection (d).

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<sup>2</sup> For a discussion of the operation of the pertinent statutes, see *Reo Motors v. Commissioner*, 338 U. S. 442.



One of the “exceptions, additions, and limitations provided in subsection (d)” is pertinent here and will be discussed later. However, at the moment it is sufficient to note that, generally speaking, the net operating loss for any given year is simply the amount by which the taxpayer’s deductions for that year exceeds income of that year.

The instant taxpayer had an excess of deductions over income, and thus a net operating loss, for 1944 only if, in computing its 1944 net operating loss, it is entitled to take a deduction for the total of \$221,610.87 it paid to the treasurer of Yolo County on “calls” made to pay the interest on bonds issued by Reclamation District No. 2035. The Tax Court held that the \$221,610.87 was deductible under Section 23 (c) (1) (E) of the Code (Appendix, *infra*) as “taxes paid”. This holding, we submit, is plainly erroneous. As we shall show, the payments aggregating \$221,610.87 were of interest rather than of taxes and, as interest, are not deductible in the circumstances of this case.

*A. The \$221,610.87 paid by taxpayer in 1944 to cover interest on the Reclamation District bonds did not constitute “taxes assessed against local benefits” and therefore is not deductible under Section 23 (c) (1) (E) of the Code as taxes allocable to interest charges*

Section 23 (c) (1) of the Code allows a deduction for taxes paid or accrued within the taxable year with certain exceptions. The exception contained in subparagraph (E) is of “taxes assessed against local benefits of a kind tending to increase the value of the property assessed”. That subparagraph also provides, however, that—

this paragraph shall not exclude the allowance as a deduction of so much of *such taxes* as is properly

allocable to maintenance or interest charges; \* \* \*.  
[Italics supplied.]

Thus, for taxpayer's payment of the \$221,610.87 to be deductible under this section, the payment must not only have been allocable to interest, as it in fact was, but must have constituted "taxes assessed against local benefits".

Strictly speaking, a tax is an enforced contribution which goes into the Government Treasury as revenue to be used to support the Government.<sup>3</sup> Thus, an assessment made for benefits received from an improvement has often been held not to constitute a "tax" in the constitutional sense.<sup>4</sup> On the other hand, the word "tax" has two meanings—one which includes and one which excludes assessments for local benefits.<sup>5</sup> Under Section 23 (c) (1) (E) assessments for local improvements are called "taxes", although they are expressly excluded from deduction as taxes.

*But a "tax" assessed against local benefits is an assessment which is levied for the purpose of defraying the cost of the improvement or, stated in another way, is levied as compensation or payment for the benefit re-*

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<sup>3</sup> *Huse v. Glover*, 119 U.S. 543, 549; *Bank of Mount Hope v. Commissioner*, 25 B.T.A. 542.

<sup>4</sup> *Board of Directors v. Reconstruction Finance Corp.*, 170 F. 2d 430 (C.A. 8th); *Northwestern etc. Co. v. St. Bd. Equal.*, 73 Cal. App. 2d 548, 166 P. 2d 917; *Santa Clara Valley L. Co. v. Meehan*, 62 Cal. App. 531, 534, 217 Pac. 787; *Bennett v. Greenwalt*, 226 Iowa 1113, 1133-1134, 286 N.W. 722; *Charlotte v. Kavanaugh*, 221 N. C. 259, 20 S.E. 2d 97; *State ex rel. v. Bishop*, 169 Or. 448, 459, 127 P. 2d 736, 129 P. 2d 276; *State ex rel. v. Drainage District v. Thompson*, 328 Mo. 728, 737, 41 S.W. 2d 941; *Lake Arthur Drain. Dist. v. Bd. Com. Chav. Co.*, 29 N. Mex. 219, 221, 222 Pac. 389; *Loomis v. Rogers*, 197 Mich. 265, 163 N.W. 1018; *Logan, Auditor v. City of Louisville*, 283 Ky. 518, 522, 142 S.W. 2d 161.

<sup>5</sup> *Johnson County Comm'rs v. Robb*, 161 Kan. 683, 690, 171 P. 2d 784; *Northwestern etc. Co. v. St. Bd. Equal.*, 73 Cal. App. 2d 548, 553, 166 P. 2d 917; *Boston Asylum, etc. v. Street Commissioners*, 180 Mass. 485, 62 N.E. 961.

ceived from the improvement.<sup>6</sup> In the usual case a municipality or other governmental subdivision will issue and sell bonds to secure funds for a particular improvement and will tax the properties benefited by the improvement to supply the funds to pay off the bonds. In such a case the assessment or "tax" paid by the property owners, whether applied to the principal of or interest on the bonds, is in payment of the cost of the improvement in proportion to the benefit received therefrom. The "tax" consists of an enforced contribution toward the cost of the improvement. In contrast, if the property owner finances and thus has already paid for the improvement, any assessment against the property owner in connection therewith is not an assessment for local benefits and thus cannot be a "tax" assessed for local benefits.

Here there was no assessment for benefits received from the drainage improvements; the "calls" by the county treasurer were not made to pay the cost of the improvements, either principal or interest. At the time the drainage improvements were made in 1924, the Conaway Ranch was owned by taxpayer's predecessor, the Birch Oil Company, *and that company constructed and financed the improvements.* Reclamation District No. 2035, which issued the bonds involved here, covered all but 1,300 acres of the Conaway Ranch, plus 240 Dis-

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<sup>6</sup> *Board of Directors v. Reconstruction Finance Corp.*, 170 F. 2d 430, 433 (C.A. 8th); *Evans v. Ockershausen*, 100 F. 2d 695, 708 (C.A.D.C.), certiorari denied *sub nom. Smith v. Ockershausen*, 306 U. S. 633; *Northwestern etc. Co. v. St. Bd. Equal.*, 73 Cal. App. 2d 548, 553, 166 P. 2d 917; *Santa Clara Valley L. Co. v. Meehan*, 62 Cal. App. 531, 534, 217 Pac. 787; *Spring Street Co. v. City of Los Angeles*, 170 Cal. 24, 29, 148 Pac. 217; *Bennett v. Greenwalt*, 226 Iowa 1113, 1134, 286 N.W. 722; *People ex rel. N. Y. School for Deaf v. Townsend*, 173 Misc. 906 (N.Y.); *Charlotte v. Kavanaugh*, 221 N.C. 259, 20 S.E. 2d 97; *Lima v. Cemetery Assn.*, 42 Ohio State 128, 130; *Vogt v. City of Oakdale*, 166 Ky. 810, 179 S.W. 1037; *Graham v. City of Saginaw*, 317 Mich. 427, 431-432, 27 N.W. 2d 42; *I.C.R.R. Co. v. City of Decatur*, 126 Ill. 92, 97, 18 N.E. 315.



trict acres which lay outside the ranch and against which the record does not show that an assessment was ever made. (See R. 347.) Since the Birch Oil Company, the owner of the ranch, was the owner of the only land which could be assessed to pay for the improvements and had in fact already paid for them, what would ordinarily be accomplished by an enforced contribution by way of a tax to pay for the improvements had already been accomplished voluntarily. The county or Reclamation District therefore was not in a position to levy a "tax" against the company to pay for the improvements and the payments made by taxpayer in 1944 were *not* in fact taxes assessed against, or to pay the cost of, the drainage improvements.

That the California statutes permitted the arrangement involved does not make the "calls" by the county treasurer demands for the payment of taxes assessed against local benefits. A demand or assessment by a political subdivision is not necessarily a "tax". See, e.g. *Mahler v. Commissioner*, 119 F. 2d 869 (C. A. 2d), certiorari denied, 314 U. S. 660; *Marx v. Commissioner*, 179 F. 2d 938 (C. A. 1st). After Reclamation District No. 2035 had been formed and had issued bonds in the amount of the cost of the drainage improvements on the land of the Birch Oil Company, that company itself held the bonds which were to be paid off through "calls" by the county treasurer against the company. Accordingly, the Birch Oil Company was both payor and payee on the bonds and interest thereon. In *Rindge Land & Navigation Co. v. Commissioner*, 2 B. T. A. 1179, the Tax Court long ago considered an arrangement of this type and stated (p. 1188) :

Where there is but one landowner, as in this appeal, a reclamation district is nothing more than a legal fiction—an instrument created to permit the owner to issue bonds for its own purposes,  
\* \* \*. [Italics supplied.]



Whatever may have been the original intended purpose of the formation of Reclamation District No. 2035 and the issuance of Reclamation District bonds, the bonds were used merely to create personal obligations of the Birches. The Birch Oil Company, which had constructed and financed the drainage improvements, was a partnership in which Mr. and Mrs. Birch, Mr. Birch's nieces (the Hopkins sisters), and Mrs. Birch's parents (the Conaways) had interests. (R. 388.) On January 1, 1924, prior to the issuance of the Reclamation District bonds, the Hopkins sisters entered into agreements under which they sold their interests to Mr. and Mrs. Birch for \$787,000 to be paid in Reclamation District bonds in the principal amount of \$786,000 and cash in the sum of \$1,000, the Birches agreeing to cause the Reclamation District to issue bonds in an amount of at least \$800,000. (R. 138.) In 1926 Mr. Birch entered into an agreement with the Conaways, Mrs. Birch's parents, for the purchase of their interest in the ranch and in the bonds of the Reclamation District, paying cash therefor. (R. 142.) Since the bonds were payable by "calls" only against the owner of the Conaway Ranch, the Birches, the bonds in the amount of \$786,000 delivered to and held by the Hopkins sisters merely represented the Birches' personal obligation to pay the purchase price of the sisters' interests in the Conaway Ranch. Such "calls" as may have been made by the county treasurer for either principal or interest on those bonds were simply "calls" for payments on the purchase price of the ranch, rather than "calls" for taxes consisting of a contribution toward the cost of the drainage improvements on the ranch, which would be leviable only against the land and had already been paid for by the then owner of the land. In 1943, after the Birches, pursuant to their agreement with the Hopkins sisters, had purchased \$476,000 par

value of the bonds delivered to the Hopkins sisters, the Birches sold \$10,000 par value of such bonds to Lulu M. Minter and \$86,000 of the bonds to the Great Republic Life Insurance Company, a corporation of which Birch was president. (R. 143.) By transferring those bonds to third parties, the Birches simply created other personal obligations in themselves, for consideration received. The bonds which they did not transfer to third parties (except to their own corporation) were bonds on which they were both payor and payee and the issuance of such bonds served no purpose whatever.

The Birches themselves treated the bonds in the hands of third parties as their personal obligation to be paid for the consideration received for delivery of the bonds to the third parties, rather than as bonds requiring payment for the drainage improvements on the Conaway Ranch. Under their agreements with the Hopkins sisters the Birches agreed that they would buy back from the Hopkins sisters, without "calls", at face value in specified annual installments, the \$386,000 in bonds they delivered to the Hopkins sisters in purchasing the sisters' interests in the Conaway Ranch and in the Birch Oil Company. (R. 390.) The Birches did in fact buy back 476 of the bonds during the first six years (R. 391) and on March 15, 1944, bought the remaining 310 bonds (R. 394). Similarly, in 1940 the Birches purchased the bonds held by the insurance company. (R. 391-392.) No amount was ever paid into the Reclamation District by the Birches or by the taxpayer-corporation (the Birches' wholly-owned corporation) for the purpose of paying off the bonds. (R. 392.) Interest payments were at first, during 1925-1930, paid by the Birches on call by the county treasurer (R. 391) but in succeeding years the Birches bought the interest coupons of the Hopkins sisters as they matured, deposited them with the county

treasurer, and received a receipt and assessment credit against the ranch and, in 1934, after the taxpayer-corporation acquired the ranch, it too purchased at face value matured interest coupons from the Hopkins sisters and from Lulu Minter (R. 391).

Payment on the bonds was previously regarded by the Tax Court as interest paid, rather than as taxes allocable to interest charges. In *Birch Ranch & Oil Co. v. Commissioner*, decided April 20, 1944 (1944 P-H T.C. Memorandum Decisions, par, 44,128), affirmed by this Court, 152 F. 2d 874, the Tax Court had before it the question of the deductibility of the interest payments made to the Hopkins sisters in 1937 and 1939. The Tax Court held the payments deductible as *interest paid*. Those interest payments were of course made directly to the Hopkins sisters and Lulu Minter, rather than through calls by the county treasurer, but the purpose of the payments was the same and the effect was also the same as if the payments had been made through calls by the county treasurer.

The incongruity of considering "calls" by the county treasurer as calls for taxes assessed to pay the cost of local improvements is even more evident when we come to the year 1944, for which taxpayer claims the taxes paid deduction. In that year (the fiscal year ending September 30, 1944) all of the 2,000 Reclamation District bonds (face value, \$2,000,000) were held by the Birches or their wholly-owned corporations except the 310 held by the Hopkins sisters for part of the year and the 10 bonds held by Lulu Minter. The calls by the county treasurer not only were not for the payment of taxes assessed to pay the cost of local improvements, either principal or interest, but the majority of the total amount paid by the taxpayer-corporation (wholly owned by the Birches) pursuant



to the calls was necessarily repaid by the county treasurer to the Birches and their other two wholly-owned corporations, the Birch Securities Company and the Birch Holding Company.

The whole arrangement—including the issuance of Reclamation District bonds on which the interest was paid in the fiscal year 1944 on “calls” from the county treasurer—was merely one which the Birches used for their own purposes, not one calling for the payment of “taxes” for public benefits. The payments made by the taxpayer-corporation were simply of interest, not of taxes allocable to interest charges representing a part of the cost of public benefits. This is true even if the Reclamation District is considered a separate entity. The existence of the Reclamation District was part of the whole arrangement, but the fact that the District may have been a separate entity cannot change the arrangement into one calling for the payment of “taxes” consisting of the cost of the drainage improvements when the cost of the improvements had in fact already been paid.

Moreover, the Congressional purpose in enacting Section 122 (d)(2) of the Code (Appendix, *infra*) requires that the total \$221,610.87 payment made by the taxpayer-corporation be treated as payment of interest and not of taxes, as we shall show under Point C, *infra*.

*B. The \$221,610.87 Is Not Deductible under Sections 23(b) and 122 (a) and (d)(2) as “Interest Paid”*

As already shown, in 1926 after the Birches had purchased the Hopkins sisters’ and the Conaways’ interests in the Conaway Ranch and the Birch Oil Company, the Birches owned the Conaway Ranch and were thus liable for payment of the Reclamation Dis-



strict bonds and interest thereon. Bonds in the amount of \$786,000 (786 bonds) had been given by them to the Hopkins sisters in the purchase of the Hopkins sisters' interests in the ranch and in the Birch Oil Company. Subsequently, the Birches, after having purchased 476 of the bonds from the Hopkins sisters pursuant to their purchase agreements with them, sold 10 bonds to Lulu Minter and 86 bonds to an insurance company. Accordingly, these bonds outstanding in the hands of third parties represented personal indebtednesses of the Birches—as to the Hopkins sisters, for the purchase of their interests and, as to Lulu Minter and the insurance company, for what were in effect loans.<sup>7</sup> The remaining 1,594 bonds were held by the Birches and merely represented an indebtedness to themselves, and thus no indebtedness at all, since they were both payor and payee on those bonds.

In 1934 the Birches organized three corporations—(1) the taxpayer-corporation, to which they transferred the Conaway Ranch and certain other property; (2) the Birch Securities Company, to which they transferred the 1,594 Reclamation District bonds (face value, \$1,594,000) they held, as well as certain stocks and other assets; and (3) the Birch Holding Company, to which they transferred all of the stock of the other two corporations and which, in return, issued 49 per cent of its stock to Birch and 51 per cent to Birch's wife. The Securities Company and the Holding Company were formed for convenience and conducted no business. The taxpayer-corporation operated the Conaway Ranch. (R. 388.) As a result of the organization of these corporations, the taxpayer-corporation became liable for interest on the indebted-

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<sup>7</sup> The Birches sold the bonds to Lulu Minter and the insurance company but, since the payment of the bonds was an obligation of the Birches as owners of the Conaway Ranch, the bonds represented the Birches' promise to repay the sale price of the bonds.

ness of the Birches to the Hopkins sisters, the insurance company and Lulu Minter, and, on the 1,594 bonds which the Birches had held and on which they were both payor and payee, the taxpayer-corporation became the payor and the Securities Company the payee. In the fiscal year 1944 the taxpayer-corporation, on "calls" by the county treasurer, paid \$221,-610.87 for interest on Reclamation District bonds and this was for interest not only on the bonds outstanding in the hands of third parties but on bonds held by the Birches, the taxpayer-corporation itself, the Securities Company and the Holding Company.<sup>8</sup>

1. *Except as to the interest paid to the Hopkins sisters and Lulu Minter, deductibility is precluded by the fact that the payment of interest was not "on indebtedness" within the meaning of Section 23 (b)*

Section 23 (b) of the Code (Appendix, *infra*) authorizes a deduction of all interest paid or accrued within the taxable year "on indebtedness" with an exception which will be noted shortly. As to the bonds other than those held in the fiscal year 1944 by the Hopkins sisters and Lulu Minter, there was no real "indebtedness".

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<sup>8</sup> In making "calls" in the fiscal year 1944, the county treasurer computed an amount which, with any balance on hand, was sufficient to provide \$60,000 for the semi-annual interest due on the bonds, and amounts paid as penalties were reflected in his computations. (R. 395.)

On September 30, 1943, the beginning of the 1944 fiscal year, the taxpayer-corporation held 86 bonds, those acquired from the insurance company; the Securities Company held the 1,594 bonds transferred to it at its organization; the Hopkins sisters held 310 bonds subject to the purchase contract with the Birches; and Lulu Minter held 10. On March 15, 1944, the Birches bought the 310 bonds from the Hopkins sisters and before the close of the fiscal year Securities was liquidated and dissolved. Thus at the close of the fiscal year 1944, the Birches held directly 310 of the 2,000 bonds; the Holding Company held 1,594 from the liquidation of Securities Company; the taxpayer-corporation held 86, and Lulu Minter 10. (R. 394.)

An indebtedness requires a creditor and debtor and those existed here only as a matter of form. The interest on bonds other than those held by the Hopkins sisters and Lulu Minter was interest payable *by* one of the Birches' wholly-owned corporations, the taxpayer-corporation, and payable *to* the Birches and their wholly-owned corporations. From a substantive standpoint, the interest paid by the taxpayer-corporation for interest on bonds other than those held by the Hopkins sisters and Lulu Minter was a payment of interest by the Birches to themselves. The payor and payees were economically identical.

In *Prudence Securities Corp. v. Commissioner*, 135 F. 2d 340 (C.A. 2d), it was held that no deduction is allowable for interest paid when payor and payee are, as here, economically ~~identical~~<sup>identically</sup>. See also *Elbert v. Commissioner*, 45 B.T.A. 685. That holding is manifestly correct, for there have been many situations in which the separate identity of a corporation has been ignored for tax purposes. Taxation is an intensely practical matter concerned with economic realities and substance controls over form.<sup>9</sup> For example, in *Higgins v. Smith*, 308 U. S. 473, it was held that the separate identity of the taxpayer's controlled corporation should be ignored in considering the tax effect of transactions between the taxpayer and the corporation. In that case the Supreme Court stated (pp. 477-478):

A taxpayer is free to adopt such organization for his affairs as he may choose and having elected to

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<sup>9</sup> *Commissioner v. Sunnen*, 333 U.S. 591; *Helvering v. Clifford*, 309 U.S. 331; *Helvering v. Stuart*, 317 U.S. 154; *Harrison v. Schaffner*, 312 U.S. 579; *Douglas v. Willcuts*, 296 U.S. 1; *Corliss v. Bowers*, 281 U.S. 376; *Burnet v. Wells*, 289 U.S. 670; *Commissioner v. Court Holding Co.*, 324 U.S. 331; *Griffiths v. Commissioner*, 308 U.S. 355; *Gregory v. Helvering*, 293 U.S. 465; *Weiss v. Stearn*, 265 U.S. 242; *United States v. Phellis*, 257 U.S. 156; *Gulf Oil Corp. v. Lewellyn*, 248 U.S. 71; *Southern Pacific Co. v. Lowe*, 247 U.S. 330.



do some business as a corporation, he must accept the tax disadvantages.

On the other hand, the Government may not be required to acquiesce in the taxpayer's election of that form for doing business which is most advantageous to him. The Government may look at actualities and upon determination that the form employed for doing business or carrying out the challenged tax event is unreal or a sham may sustain or disregard the effect of the fiction as best serves the purposes of the tax statute. To hold otherwise would permit the schemes of taxpayers to supersede legislation in the determination of the time and manner of taxation. It is command of income and its benefits which marks the real owner of property.

When the corporate entities of the Birches' wholly-owned corporations are ignored, as they should be, only the interest paid by the taxpayer-corporation on the bonds held by the Hopkins sisters and Lulu Minter was paid "on indebtedness" and is deductible.

2. *Except as to the interest paid to the Hopkins sisters and Lulu Minter, deductibility is precluded by the fact that section 122 (d)(2) was intended by Congress to prevent the deduction of interest paid to carry tax-exempt bonds to the extent that no economic loss was sustained by the payment of such interest*

There is still another reason why the taxpayer-corporation's payments of interest in the fiscal year 1944 are not deductible (except in part) and it is a reason which makes it clear beyond any doubt that the instant situation is of a type requiring that the separate entity of the Birches' wholly-owned corporations should be ignored.



Although Section 23 (b) of the Code authorizes a deduction for interest paid on indebtedness, an exception is made in the case of interest paid—

on indebtedness incurred or continued to purchase or carry obligations \* \* \* the interest upon which is wholly exempt from the taxes imposed by this chapter.

This provision is also treated specially for carry-back deduction purposes. As already stated, the “net operating loss” of any particular year is defined in Section 122 (a) as meaning the excess of deductions over the gross income for that year “with the exceptions, additions, and limitations provided in subsection (d)”. Those exceptions, additions, and limitations include the following:

(2) There shall be included in computing gross income the amount of interest received which is wholly exempt from the taxes imposed by this chapter, decreased by the amount of interest paid or accrued which is not allowed as a deduction by section 23 (b), relating to interest on indebtedness incurred or continued to purchase or carry certain tax-exempt obligations; \* \* \*

When Congress enacted the net operating loss deduction provisions in 1939, it stated its intent with respect to these exceptions, additions and limitations to be as follows (H. Rep. No. 855, 76th Cong., 1st Sess, p. 17 (1939-2 Cum. Bull. 504, 517)):

The net operating loss deduction is the net operating loss carry-over reduced by certain adjustments intended to prevent net losses from being used as a deduction by the taxpayer where he is not suffering any *economic* loss by reason of the fact that his income contains nontaxable items (as in the case of percentage depletion, *exempt interest on State and local bonds*, and, with respect to corporations, intercorporate dividends, and interest on partially exempt Federal obligations).

*The exceptions and limitations provided in section 122 (d) are for the purpose of insuring that only an ECONOMIC loss will be taken into account. It is provided that in computing gross income, wholly tax-exempt interest, diminished by the amount of interest paid or accrued not allowed as a deduction by section 23 (b), relating to interest on indebtedness incurred or continued to purchase or carry certain tax-exempt obligations, shall be included, \* \* \* [Italics supplied.]*

The interest received by holders of the Reclamation District bonds was tax-exempt interest, as Mr. Birch himself testified. (R. 286; see also, R. 58, 86, 166, 183, 186, 187, 188.) The interest paid by the taxpayer-corporation was of course paid to carry the bonds, and thus paid to carry "obligations \* \* \* the interest upon which is wholly exempt from the taxes imposed by this chapter" within the meaning of Section 23 (b) of the Code. Cf. *First Nat. Bank v. United States*, 283 U. S. 142.

The Birches sustained no *economic* loss by payment of interest on the bonds, through the taxpayer-corporation, on "calls" of the county treasurer, to the extent that the interest was repaid to the Birches either individually or through their wholly-owned corporations, the Birch Securities Company and the Birch Holding Company. And, since it was the Congressional purpose to allow a deduction of interest paid to carry tax-exempt bonds only to the extent that an *economic* loss was sustained, it necessarily follows that the separate entity of the taxpayer-corporation, the Birch Securities Company and the Birch Holding Company should be ignored in computing net operating loss of the taxpayer-corporation for the fiscal year 1944. By Section 122 (d)(2) Congress intended that the interest paid to carry tax-exempt bonds should be deductible only against the interest received from such bonds. The tax-

payer-corporation did not report the tax-exempt interest received by the Birches, the Birch Securities Company, the Birch Holding Company, nor apparently even by itself, and accordingly is not entitled to deduct interest paid to carry the bonds on which the tax-exempt interest was received.

It is not entirely clear that the interest paid by the taxpayer-corporation on the bonds held by the Hopkins sisters and Lulu Minter is deductible. That interest was also in a sense paid to carry tax-exempt bonds. On the other hand, the bonds held by Hopkins sisters and Lulu Minter really represented personal obligations of the Birches and the Birches received no tax-exempt benefit from interest paid on those bonds. From the standpoint of substance, the situation with respect to those bonds was the same as if the Birches were paying interest on indebtedness consisting of the purchase price of the Hopkins sisters' interest in the Conaway ranch and on a loan from Lulu Minter. We therefore do not contend that the interest paid to the Hopkins sisters and Lulu Minter during the fiscal year 1944 was not deductible.<sup>10</sup>

*C. The Tax Court's holding that taxpayer's total \$221,610.87 payment is deductible as taxes paid is in conflict with the purpose of Section 122 (d)(2)*

As has been seen, Congress intended by Section 122 (d)(2) to insure that only *economic* losses would be taken into account in computing net operating loss for the purpose of a carry-back deduction to a prior year. Even if the aggregate \$221,610.87 payment made by

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<sup>10</sup> In the previous case relating to the deductibility of interest paid by the taxpayer-corporation, the Tax Court held that the interest paid to the Hopkins sisters during the years 1937 and 1939 was deductible. The Commissioner did not contend that such interest was not deductible because paid to carry tax-exempt bonds.

taxpayer in the fiscal year 1944 may be regarded as a payment of "taxes", it must be recognized that the arrangement resulting in the payment was unusual and not of the type commonly deemed to require the payment of "taxes". For present purposes, there is no reason to extend the deduction for taxes paid to such an arrangement; on the contrary, to do so is to thwart the Congressional purpose of Section 122 (d) (2). The Birches made the total \$221,610.87 payment, through the taxpayer-corporation, and also received most of it back, either individually or through the Securities Company and Holding Company. Since the part they received back was tax-exempt interest, to hold that the taxpayer-corporation is entitled to deduct the total payment as a payment of "taxes" is to allow a deduction for that which was *not* an economic loss, contrary to the purpose of Section 122 (d) (2). The Congressional intent should always be effectuated if possible. It can be in the present case by a holding, amply justified, that the total \$221,610.87 payment made by the taxpayer-corporation was not of, or should not be treated as of, taxes—that it was, or at least should be treated as, interest and as interest is not deductible in computing net operating loss.

#### CONCLUSION

The decision of the Tax Court is incorrect and should be reversed.

Respectfully submitted,

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NOVEMBER, 1950.



## APPENDIX

## Internal Revenue Code:

## SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

\*                      \*                      \*                      \*                      \*

(b) *Interest*.—All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from the taxes imposed by this chapter.

(c) [as amended by Sec. 202 (a) of the Revenue Act of 1941, c. 412, 55 Stat. 687, and Sec. 111 of the Revenue Act of 1943, c. 63, 58 Stat. 21] *Taxes Generally*.—

(1) *Allowance in general*.—Taxes paid or accrued within the taxable year, except—

\*                      \*                      \*                      \*                      \*

(E) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges; and

\*                      \*                      \*                      \*                      \*

(s) [as added by Sec. 211(a) of the Revenue Act of 1939, c. 247, 53 Stat. 862] *Net Operating Loss Deduction*.—For any taxable year beginning after December 31, 1939, the net operating loss deduction computed under section 122.

(26 U. S. C. 1946 ed., Sec. 23.)

SEC. 122 [as added by Sec. 211 (b) of the Revenue Act of 1939, *supra*] NET OPERATING LOSS DEDUCTION.

(a) [as amended by Sec. 105 (e) (3) (A) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Definition of Net Operating Loss*.—As used in this section, the term “net operating loss” means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions, and limitations provided in subsection (d).

(b) [as amended by Sec. 153 (a) of the Revenue Act of 1942, *supra*] *Amount of Carry-Back and Carry-Over*.—

(1) *Net operating loss carry-back*.—If for any taxable year beginning after December 31, 1941, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-back for each of the two preceding taxable years, except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the second preceding taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such second preceding taxable year without regard to such net operating loss.

\* \* \* \* \*

(d) [as amended by Sec. 105 (e) (3) (C) of the Revenue Act of 1942, *supra*] *Exceptions, Additions, and Limitations*.—The exceptions, additions, and limitations referred to in subsections (a), (b), and (c) shall be as follows:

\* \* \* \* \*

(2) There shall be included in computing gross income the amount of interest received which is

wholly exempt from the taxes imposed by this chapter, decreased by the amount of interest paid or accrued which is not allowed as a deduction by section 23 (b), relating to interest on indebtedness incurred or continued to purchase or carry certain tax-exempt obligations;

\* \* \* \* \*

(26 U. S. C. 1946 ed., Sec. 122).

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.23(c)-3. *Taxes for Local Benefits.*—So-called taxes, more properly assessments, paid for local benefits, such as street, sidewalk, and other like improvements, imposed because of and measured by some benefit inuring directly to the property against which the assessment is levied, do not constitute an allowable deduction from gross income. A tax is considered assessed against local benefits when the property subject to the tax is limited to property benefited. Special assessments are not deductible, even though an incidental benefit may inure to the public welfare. The real property taxes deductible are those levied for the general public welfare by the proper taxing authorities at a like rate against all property in the territory over which such authorities have jurisdiction. Assessments under the statutes of California relating to irrigation and of Iowa relating to drainage, and under certain statutes of Tennessee relating to levees, are limited to property benefited, and if the assessments are so limited, the amounts paid thereunder are not deductible as taxes. The above statements are subject to the exception that in so far as assessments against local benefits are made for the purpose of maintenance or repair or for the purpose of meeting interest charges with respect to such benefits, they are deductible. In such cases the burden is on the taxpayer to show the allocation of the amounts as-

sessed to the different purposes. If the allocation cannot be made, none of the amounts so paid is deductible.

SEC. 29.122-1. *Net Operating Loss Deduction.*—

(a) *General.*—Section 122 provides the rules for the computation of the net operating loss deduction allowed by section 23 (s). The net operating loss deduction is the aggregate of the net operating loss carry-overs and carry-backs to the taxable year, reduced by certain adjustments to prevent the deduction of losses absorbed by income not taxed.

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No. 12639

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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COMMISSIONER OF INTERNAL REVENUE,

*Petitioner,*

*vs.*

BIRCH RANCH AND OIL COMPANY,

*Respondent.*

ON PETITION FOR REVIEW OF THE DECISION OF THE  
TAX COURT OF THE UNITED STATES.

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## BRIEF FOR THE RESPONDENT.

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## BRIEF FOR THE RESPONDENT.

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### The Opinion Below.

The findings of fact and opinion of the Tax Court are set forth at R. 385-408 and are reported at 13 T. C. 930.

### Jurisdiction.

The jurisdiction is as stated in Appellants' Brief.

### Question Presented.

The question presented is as set forth in Appellants' Brief and is as follows:

1. "Whether the circumstances of the case are such as to entitle the taxpayer-corporation to a 'taxes paid' deduction under Section 23(c) of the Internal Revenue Code, or to an 'interest paid' deduction under Sections 23(b), 122(a) and (d) (2), in computing its 1944 net operating loss for the purpose of a carry-back deduction in the taxable year 1942 under Sections 23(s) and 122."



It seems to respondent, the following questions are also presented:

2. Where a reclamation district is regularly formed by a group of eight property owners, including the Birches, and where bonds covering the district are regularly issued and nearly one-half thereof is owned by various persons other than Birches and are dealt in for value over a period of nearly twenty years, does such district, and do such bonds, lose their bona fide character by reason of the acquisition by respondent corporation, as the Birches' successor in interest, of practically all of the land in the district, and by reason of the Birches' gradual acquisition of all of such bonds over such period?

3. Where Mr. Birch was nearly 70 years old and during the depression could not get bank credit sufficient to enable him to operate the ranch unless he placed the title thereof in a corporation, and where the taxpayer corporation was formed for the purpose of securing bank credit, is not the corporation a separate legal entity, and does not this fact furnish an additional reason as to why it is entitled to deduct as taxes all assessments paid by it to the County Treasurer covering its lands, irrespective of who owns the bonds?

### **Statute and Regulations.**

The statute and treasury regulations are set forth in the Appendix to Appellants' Brief. Appellant, however, fails to set forth the pertinent portions of the California statute applicable to reclamation districts and the issuance of reclamation bonds. The applicable portions of this statute are set forth in an Appendix to this brief. (Pt. 3, Tit. 8, Ch. 1, Art. 2, Secs. 3478 and 3480.)

### Statement of the Case.

Appellants correctly set forth in their brief the Tax Court's findings of fact. [R. 387-397.] The Stipulation of Facts, the exhibits (separately transmitted by stipulation) and the testimony of respondents' witnesses, are also pertinent as additional facts which support the Tax Court's opinion and conclusions of law.

The Stipulation of Facts appears at R. 134-147. The testimony of respondents' witnesses appears at R. 211-349.

The respondents' exhibits were admitted at the following pages in the record and consist of the following:

Page 197	Exhibit 1—photostatic copy of report of Commissioner with respect to taxpayer.
Page 201	Exhibit 2—findings of fact of Judge Turner in former case.
Page 202	Joint Exhibit 3a—respondents' income tax return for the year ending September 30, 1944.
Page 206	Exhibit 5—judgment roll finding formation of reclamation district 2035 to be sufficient and legal.
Page 206	Exhibit 6—judgment roll finding first bond issue sufficient and legal.
Page 209	Exhibit 7—judgment roll finding refunding bond issue sufficient and legal.
Page 210	Exhibit 8—copy of cancelled bond No. 2000 of first issue.

*Respondents' Exhibits.*

- Pages 215-219 Exhibits 9 to 12—calls of County Treasurer with respect to assessments against reclamation district, correspondence relating thereto, and taxpayers' payment as taxes totaling the said sum of \$221,610.87, being the amount referred to in said Exhibit 2 and being the item of deduction involved in the within action.
- Page 274 Joint Exhibit 13f—return for year ending September 30, 1942.
- Page 278 Exhibit 14—first Hopkins contract.
- Page 279 Exhibit 15—second Hopkins contract.

*Appellants' Exhibits.*

- Page 228 Exhibit B—letter produced by Mr. Landrum regarding payment of assessment.
- Page 230 Exhibit C—correspondence between respondent and County Treasurer.
- Page 232 Exhibit D—ditto.
- Page 234 Exhibit E—letters relating to call No. 23, showing payment of call by means of interest coupons as permitted by statute.

The findings of fact of the Tax Court taken as a whole, and the aforesaid evidence and stipulation would seem to impel the following conclusions: (1) reclamation district 2035 is a bona fide reclamation district and state agency and a separate legal entity, entirely distinct from

the land owner within the district; (2) the \$2,000,000 reclamation bonds were regularly issued and are valid and existing bonds, the principal of which, together with its interest thereon, constitutes a lien against all lands of the district until paid; (3) respondents' payments to the County Treasurer, or its purchase of the interest coupons and the bonds and the delivery of such to the County Treasurer, under the Reclamation Act constituted payment of taxes and not interest; (4) and that respondent is not economically identical with the district or the bonds.

In its opinion the trial court stated in part as follows:

“The essential factual premises or inferences which respondent assumes for this argument are not adequately supported by the evidence.” [R. 403.]

For the reason that respondent has disregarded essential and material facts of the case, it will be helpful if we quote here from a portion of the partial stipulation of facts, with appropriate emphasis added, as follows:

“6. Desiring to reclaim and develop the lands comprising the Conaway Ranch, the Birch Oil Company, in 1918, filed a petition with the Board of Supervisors of Yolo County, California, for the creation of a reclamation district which would include 24,210 acres and would cover the whole of the Conaway Ranch and twenty-odd other parcels of land not owned by the Birch Oil Company or its members. In April 1919, the establishment of Reclamation District No. 2035, comprising approximately 21,000 acres, was approved by the Board of Supervisors. *Excluded from the district as approved were some 1,300 acres of the Conaway Ranch and all except eight of the twenty-odd other parcels of land not owned by the Birch Oil Company or its members.*” [R. 136.]



“7. Organization of the district was completed and the County Board of Supervisors appointed Conaway, C. Harold Hopkins, and a man named Armfield as trustees for the district. In June 1919, the trustees employed an engineer and directed him to prepare plans for the reclamation and irrigation of lands in the district, with estimates of the cost of the necessary improvements. In June, 1920, the trustees approved the plans submitted by the engineer and his estimate of \$2,264,740 as the cost of the improvements. The plans submitted called for the construction of the main levee along the edge of the Yolo By-pass, as above described. The plans were approved by the Reclamation Board of the State of California in October 1920, and in December of the same year, by the Board of Supervisors. Commissioners of assessment were appointed to assess the value of the benefits to the lands in the district from the improvements contemplated and to apportion the cost of said improvements according to the benefits that would accrue to each tract of land in the district. Thereafter, and prior to July 2, 1924, the commissioners made the assessment and apportionment for which they were appointed. The assessment was approved by the Board of Supervisors on July 23, 1924; and the list of assessment was filed on the same day with the County Treasurer of Yolo County.” [R. 137.]

“8. The Birch Oil Company, under the direction of the district’s engineer, built the improvements called for in the reclamation plan and financed all the costs, which were slightly in excess of two million dollars. The work was substantially completed by 1925, at which time the improvements consisted of 45 miles of roadways, 47 miles of irrigation canals, 55 miles of drainage canals and ditches, and included

bridges, pumping plants and other structures necessary for the development of the lands in the district. By 1925 Birch had acquired individually and at undisclosed costs seven of the eight parcels of land which with the Conaway Ranch comprised the land of the district. The parcel not so purchased consisted of 240 acres." [R. 138.]

"9. In the meantime, the Hopkins sisters, being desirous of disposing of their interests in the Conaway Ranch, by agreements dated January 1, 1924, sold such interests to Birch and Mrs. Birch for \$787,000, an amount designed to pay them their proportionate part of the Birch Oil Company funds invested in the ranch. Under the agreements each of the sisters agreed to accept bonds of Reclamation District No. 2035 in the principal amount of \$393,000 and cash in the sum of \$500. Birch and his wife agreed to cause the district to issue bonds in an amount of at least \$800,000, which were to constitute a prior lien on all of the property in the district, and further promised to deliver on or before February 1, 1925, to each of the sisters the amount of the bonds and cash called for by the agreements. Birch and his wife were to have immediate and absolute possession and control of the properties acquired from the Hopkins sisters and were to be entitled to all rents and profits of every kind therefrom and were to assume all liabilities and burdens incident to the ownership thereof. The bonds not having been issued at the time of the agreements of January 1, 1924, Birch gave to each of the sisters his promissory note in an amount equal to the amount of the bonds she was entitled to receive under the agreements. The notes were to run for 10 years and were to draw interest at 6 per cent per annum from January 1, 1924, for

a period of 5 years, and at 7 per cent thereafter. Birch had the option of paying the notes in full at any time prior to the expiration of the 10 year period." [R. 139.]

"10. According to the minutes, the landowners, at an election held on August 28, 1924, voted to issue bonds to pay for the reclamation work which had been done, and on October 26, 1924, the trustees adopted resolutions providing for the issuance of the bonds." [R. 139.]

"11. On January 5, 1925, the trustees of the district adopted resolutions directing that the district pay Birch and Conaway \$2,000,000 for moneys advanced in the construction of the improvements; that Warrant No. 1 of the district be issued to them in that amount; that the bonds of the district be placed in the hands of the County Treasurer; and that the County Treasurer be requested to advertise the bonds for sale at the earliest possible date. On the same day Warrant No. 1 for \$2,000,000, drawn on the Treasurer of Yolo County, was issued to Conaway and Birch. The warrant was approved by the Board of Supervisors of Yolo County and was presented for payment to the County Treasurer but was not paid for want of funds." [R. 139.]

"12. On January 7, 1925, the trustees of the district delivered to the County Treasurer bonds of the district totaling \$2,264,740. The bonds were dated January 1, 1925, and bore interest at the rate of 6 per cent per annum until paid. They were in denominations of \$1,000. The first \$227,000 thereof were to mature on January 1, 1935, with a like amount maturing on January 1 of each year following until January 1, 1944, when the bonds then remaining and amounting to \$221,740, were to mature. Also on

January 7, 1925, the County Treasurer gave notice that on January 23, 1925, he would sell Bonds Nos. 1 to 2,000, inclusive, of \$2,000,000 par value, to the highest bidder, and stated that outstanding warrants of the district, with accrued interest thereon, would be accepted in payment for the bonds. Birch, acting for himself, Mrs. Birch and the Conaways, was the highest bidder, his bid being \$2,000,000 plus accrued interest. Being the highest bidder, he became the purchaser of the bonds and gave in payment therefor Warrant No. 1 of the district, which had been received by him and Conaway in payment for the building of the improvements for the district." [R. 140.]

"13. Upon receipt of the bonds of the district, Birch delivered to each of the Hopkins sisters \$393,000 par value of such bonds, or a total of \$786,000, pursuant to the agreements of January 1, 1924, whereunder he and his wife had acquired from the Hopkins sisters all of the interests of the latter in the Conaway Ranch. Upon delivery of the bonds, the Hopkins sisters delivered to Birch the promissory notes covering the purchase price of their interests in the ranch which had been received from him at the time of the January 1, 1924 agreements. At the same time they made formal conveyance to Birch and his wife of all their interests in the Conaway Ranch." [R. 140.]

"14. At or about the same time and pursuant to the terms of agreements dated January 10, 1925, the Hopkins sisters granted to Birch and his wife the right to purchase the bonds received by them as above set forth, at the prices and on the terms set forth in the said agreements. According to these agreements, Birch and his wife offered and agreed to purchase at face the bonds in question, the purchases



from each sister to be made in installments of \$39,300 on January 1, 1926, and on January 1 of each year thereafter until January 1, 1933, with a final installment of \$78,600 on January 1, 1934, and on each purchase date to buy all matured coupons appertaining to the bonds covered in the particular installment. At each installment date the sale of the bonds by the Hopkins sisters to Birch and his wife was to be completed at the option of the Hopkins sisters. To assure payment for the respective installments of the bonds, Birch and his wife agreed to deliver to B. F. Conaway and C. Harold Hopkins, as trustees, the balance of the district's outstanding bonds in the amount of \$1,214,000, and upon default in the payment of any of the above installments, the Hopkins sisters were to be permitted to sell, or have sold, so much of the bonds held in trust as should be required to pay the amount in default. The trustees might also release to Birch and his wife such of the bonds as might be required by them as a pledge for money borrowed to pay any current installment. Otherwise the bonds held in trust were to be released by the trustees only upon the written consent of the Hopkins sisters or upon full performance of the agreements by Birch and his wife. In the event the Hopkins sisters should elect at any installment date not to sell the bonds called for by the agreements, Birch and his wife had the option to declare the agreement at an end. Provision was also made that Birch and his wife, on 90 days notice, might elect to buy bonds in advance of the regular installment dates provided and similarly might declare the entire agreement at an end if the Hopkins sisters should reject the offer. In respect of all purchases prior to January 1, 1929, Birch and his wife were to pay interest at the rate of six per cent, the rate called for by bonds. On pur-

chases after that date, they were obligated to pay seven per cent or one per cent over the interest provided for in the bonds.” [R. 142.]

“15. In 1926 Birch entered into an agreement with the Conaways for the purchase of their interests in the ranch and in the bonds of Reclamation District No. 2035. The purchase price was paid in cash and in installments.” [R. 142.]

“16. Beginning with January 1, 1926, the first installment date under the agreements of January 10, 1925, the Hopkins sisters elected to sell the bonds to Birch and his wife pursuant to the terms of the said agreements. Birch and his wife made the payments on the bond purchases as called for in the agreements and as elected by the Hopkins sisters until the early 1930's, when, due to the depression and a resulting lack of funds, they were unable to make the further payments on the dates prescribed, and extensions of time have thereafter been allowed. The bonds paid for in the face amount of \$476,000 were delivered to Birch and his wife. The Hopkins sisters, in April, 1943,\* still held the remaining \$310,000 of the said bonds, but still held Birch and his wife liable on their obligations under the agreements of January 10, 1925. Their interest is in the receipt of the cash payments provided for in the contracts and they are unwilling to accept anything else. Of the \$476,000 par value of the bonds paid for by Birch and his wife and received from the Hopkins sisters, \$10,000 par value of such bonds were sold to Lulu M. Minter and \$86,000 passed into the hands of the

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\*On April 5 and 6, 1943, the Tax Court heard the case of *Birch Ranch and Oil Company*, Docket 109993, Memorandum Opinion entered April 20, 1944, which related to the years 1937 and 1939.

Great Republic Life Insurance Company, a corporation of which Birch was president. There was later a dispute between petitioner and the insurance company over rights of petitioner in and to the said bonds, the exact basis for which dispute is not shown." [R. 143.]

"17. On October 15, 1934, Birch and his wife organized Birch Ranch and Oil Company, the petitioner herein, and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000. Birch had been having difficulties during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, and *the petitioner was organized for the purpose of procuring needed bank credit.*" [R. 144.]

In his findings of fact in his preceding case, No. 19059 [Exhibit 2 herein] Judge Turner found as follows:

"In a proceeding brought by the trustees to determine the legality of the district, the Superior Court of California in and for the County of Yolo, in June, 1920, entered its judgment that Reclamation District No. 2035 is 'a duly and regularly organized and legal Reclamation District.' " [Exhibit 2, p. 86.]

\* \* \* \* \*

"In a proceeding brought by the trustees of the district, the Superior Court of California, in and for the County of Yolo, on March 2, 1925, entered its judgment 'that said bonds are a valid legal obligation of said Reclamation District No. 2035.' " [Exhibit 2, p. 89.]

\* \* \* \* \*

"Beginning in 1925, up to and including 1934, Birch and his wife for the Conaway Ranch formally paid over \$120,000 per year for disbursement as interest on the bonds of Reclamation District No. 2035. Such portion of the amount so paid as was applicable to bonds owned by Birch and his wife was repaid to them, but under a claim that interest on such bonds was tax exempt, the amounts so received were not reported by them as taxable income. In each of the said years, Birch and his wife, on their income tax returns, claimed a deduction of \$120,000 as interest paid. *The propriety of these deductions was questioned by the Bureau of Internal Revenue for practically every year, but in each instance the deduction was ultimately allowed.*"\* (Emphasis added.)

"On October 15, 1934, Birch and his wife organized Birch Ranch and Oil Company, the petitioner, herein, and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000. Birch had been having difficulties during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, *and the petitioner was organized for the purpose of procuring needed bank credit.*" [Said Exhibit 2, p. 93.] (Emphasis added.)

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\*This was before the incorporation of the Birch Ranch and Oil Company and the Birch Securities Company and while the Birches owned all the land except 240 acres and all the bonds except those owned by the Hopkins, Miss Minter and the Republic Life.



The Superior Court of Yolo County by a judgment duly rendered determined that the refunding bonds issued in 1935 are a valid legal obligation of said Reclamation District 2035. [Exhibit 7 herein.]

Through respondents' witnesses the following facts were also established:

Over a period of years commencing in 1925 and ending in 1946, the bonds of the entire bond issue were dealt in at their face value as to both principal and interest with one minor exception, with respect to 86 shares. [Stipulation of Facts, *supra*, and R. 262, 267, 276, 277, 280, 285, 306, 309, 314, 315, 317, 318, 319, 321 and 324.]

During the five years following 1920, Mr. and Mrs. Birch acquired seven of the eight parcels of land which were included in the district by the Board of Supervisors and which were not a part of the Conaway ranch. [R. 136.]

At the time of the incorporation of the Birch Ranch and Oil Company, Mr. and Mrs. Birch owned \$1,594,000 of the bonds; the Hopkins, \$310,000; Lulu Minter, \$10,000; and the Great Republic Life Insurance Company, \$86,000. [R. 277.]

The Birch Securities Company finished the purchase of the balance of the Hopkins bonds in March, 1944, at a price equal to the par value of the bonds. [R. 280.]

By 1946 the Birchs had acquired all of the bonds and sold them at par to a Mr. Rasmussen. [R. 316.]

No bonds were ever sold or dealt in at less than par, except the Great Republic Life Insurance Company 86 bonds, which were sold for \$65,000. [R. 276.]

In the stipulation it says: "Beginning with 1937 and until 1943, no amount has been paid in any year by petitioner (respondent herein) as interest on the 1,594,000 of such bonds transferred by Birch and wife to the Birch Securities Company." That statement is incorrect in that "it seems that the common expression is that we pay interest into the County Treasury to pay the interest on the bonds, whereas the proper notation and entry would be that we pay the assessment that is levied by the district to meet the interest on the bonds." [R. 284.]

For the first six years of the Hopkins contract, beginning with 1925, the Hopkins collected the interest on the bonds through their collection from the County Treasury on the coupons that matured on the bonds. Mr. and Mrs. Birch paid the assessment based on the call from the County Treasurer on the bonds. This provided for the interest payment, and the Hopkins cashed their coupons. [R. 285.]

From 1931 to 1934, Mr. and Mrs. Birch purchased the coupons from the Hopkins by paying the face value of the coupons as they matured. They turned the coupons in to the County Treasurer, keeping in mind the provisions of the statute. (Appendix B herein, providing for the interest coupons to be turned in to the County Treasurer in payment of assessments the same as money.)

Exhibit One is the usual form of receipt from the County Treasurer of payment upon either turning in coupons or turning in money. [R. 286.]

When Mr. and Mrs. Birch received back from the County Treasurer interest in their coupons, they did not take that into account as part of their income, as it was exempt income. From 1925 to 1934 while they personally

owned those bonds this procedure was questioned every year by the Commissioner and was never disapproved. [R. 287.]

The reference in the stipulation to the bonds owned by the Birch Ranch and Oil Company and the Great Republic Life Insurance Company not being paid by April, 1936, is incorrect. All assessments were paid up until 1937, but subsequent to that, up to 1943, no payments were made. This was because the company was unable to raise any funds. It did not have the money and could not borrow any. The depression period was still on at that time. The bank that we had our account in at Sacramento failed and tied up our funds. [R. 288.]

All assessments of the Reclamation District were paid during the fiscal year ending September 30, 1944. [R. 290.]

At that time the Birches companies were in a little different financial shape, and were able to take care of the various obligations. [R. 290.]

The stipulation on page 14 reads that: "on its books for the fiscal years 1937 and 1939 the Birch Ranch and Oil Company accrued \$120,000 to represent (interest) on the entire two million par value of issued bonds." That statement is incorrect. [R. 292.]

The company had employed a bookkeeper to open up the corporation books, and he interpreted that payment as a payment of interest, rather than a payment of an assessment, and he treated the payment to the Hopkins as paying them interest on our obligations under the contract, rather than paying the assessment so that the Hopkins could cash the coupons that matured at that time. It was not discovered that it was handled that way until the

question was raised by a field agent of the government. [R. 295.]

In participating as one of the landowners in the formation of the Reclamation District No. 2035, the Birches did not have any intention of tax avoidance. The fact never occurred to them. [R. 297.]

Mr. and Mrs. Birch and Mr. and Mrs. Conaway in performing the contract for the improvements of the Reclamation District spent an amount in excess of \$2,000,000, for which they received the warrant in that amount. [R. 297.] They did not get the bonds until six or seven years later. [R. 298.]

The Birch Ranch and Oil Company was a party to the agreement in selling the ranch and Mr. and Mrs. Birch to the agreement for selling the bonds. [R. 306.]

At the time the Birch Securities Company was incorporated in 1934 it received \$1,594,000.00 in bonds. [R. 309.]

Mr. and Mrs. Birch personally guaranteed Mr. Rasmussen under the option that they would be able to deliver all of the bonds. They were contemplating dissolving the Birch Securities Company, and therefore the bonds would come back to Mr. and Mrs. Birch. By July 1, 1946, the option was exercised. By that time the dissolution of the Birch Securities Company had taken place, and Mr. and Mrs. Birch owned all the bonds. [R. 316.]

By March 15, 1944, the Hopkins agreements were marked "cancelled." By this time the Birches had paid the Hopkins the sum of \$260,000 in cash, which was for the balance of the Hopkins bonds. [R. 321.]

In 1943 there was a large amount of unpaid interest on the bonds, but the County Treasurer was not doing



anything about that, as far as foreclosing on the land was concerned. If they did not make any calls, there wasn't any default. [R. 328.]

The County Treasurers all over the state generally were doing this to help out the land owners. [R. 261.]

Exhibits 9, 10, 11 and 12 relate to calls made by the County Treasurer and payments made by respondent. The first calls were made to cover coupons that had matured. After all past due coupons had been redeemed, then regular calls were made for the current accumulation and maturity of the interest on the bonds. [R. 329.]

The reason payments were made in 1943 and 1944 was not simply because the company's bookkeeping was on a cash basis. The reason was because the company was able to raise the funds to pay them. Prior to that time, during the depression, it could not even pay the county taxes, or the assessments, on the Reclamation District. [R. 331.]

The company did not borrow money to pay an assessment. The loans it got from the bank were for the operation of the ranch, and not for the purpose of paying an assessment. [R. 332.]

At the time of the Rasmussen transaction, all of the coupons were paid, but the bonds had not been paid for in full to the Hopkins. [R. 332.]

All the arrears of the past due coupons were taken up by 1944. [R. 333.]

In June, 1946, there were several payments to the County Treasurer aggregating \$474,272.53. That was closing up everything that was due and past due on the bonds. [R. 333.]

The fact that bonds which are issued are tax exempt, did not enter into reason for the organization of the Reclamation District. [R. 334.]

The reason that the bonds were not paid off and were refunded was that we did not have the funds to pay the bonds and it was a common practice for all districts to refund bonds from time to time. That is provided for in the statute. [R. 335.]

The first bond issue came due in 1935, and we were under quite a depression at that time. The company could not meet the payments, and therefore the only alternative was to have a new bond issue. [R. 335.]

At the time of the organization of the district, Mr. Birch did not receive any advice from any attorney or accountant with respect to the tax phase of the matter. The Birches did not have any thought in mind of ever getting out a bond issue. That matter first came to their attention after they received the bonds in 1925. They did not know of that feature before that time. [R. 338.]

The Hopkins never at any time permitted any of the interest coupons to become past due. All interest coupons on the bonds owned by the Hopkins were purchased by the Birch Ranch and Oil Company as they became due. [R. 262.]

Also the coupons of the bonds owned by Miss Minter. All these coupons were turned into the County Treasury under the provisions of Section 3482, which provides they may be turned in the same as money. [R. 263.]

The coupons were always purchased for the full face value. [R. 267.] Also in every instance except as to the 86 Republic Life bonds the bonds were dealt in at their full face value. [R. 276.]

## ARGUMENT.

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### POINT ONE.

The Tax Court Did Not Err in Holding That the Payments Involved Are Deductible for the Reason That Under the Facts of This Case Such Payments Were Bona Fide Payments of Taxes Assessed Against Local Benefits Made for the Purpose of Meeting Interest Charges With Respect to Such Benefits.

The Tax Court stated in its opinion as follows:

“By section 23(c)(1), Internal Revenue Code, taxes paid or accrued within the taxable year are deductible except:

(E) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges; \* \* \*

As all of the \$221,610.87 paid to the County Treasurer was for application to interest charges, none of it is excluded as a deduction by the statutory exceptions, and respondent does not contend that it was.”  
[R. 400.]

Attention should also be directed to the fact that Treasury Regulations III set forth at page 34 of Appellant's Brief, with respect to deductions similar to those involved here, provide as follows:

“Assessments under the statutes of California relating to irrigation and of Iowa relating to drainage, and under certain statutes of Tennessee relating to

levees, are limited to property benefited, and if the assessments are so limited, the amounts paid thereunder are not deductible as taxes. *The above statements are subject to the exception that in so far as assessments against local benefits are made for the purpose of maintenance or repair or for the purpose of meeting interest charges with respect to such benefits, they are deductible."*

This rule is recognized by and interpreted in the opinion in the case of *Andrew Little*, 21 B. T. A., 911-915, in which it is held that interest on reclamation bonds is deductible as taxes within the meaning of a similar section which existed as part of the Revenue Act of 1921.

It would seem that the facts stated in the preceding statement of the case and in the stipulation of facts [R. 134-147] uncontrovertibly establish that the assessments which are the basis for the deduction involved herein were made for the purpose of meeting interest charges with respect to local benefits within the provisions of the above-quoted regulations.

In his Opening Brief, appellant claims that the deduction involved herein is not proper because "here the improvements involved were paid at the outset by the only party against whom taxes could otherwise have been levied to pay for the improvements." He also claims that "the whole arrangement, although authorized by the law of California, was merely one through which the Birches had reclamation district bonds issued for their own purposes in which they used it to create personal indebtedness." He claims that "there was no assessment for benefits received from the drainage improvements"; (because) "at the time the drainage improvements were made in



1924, the Conaway Ranch was owned by taxpayer's predecessor."

The Statement of Facts heretofore presented established that the facts of the case are contrary to these statements. Appellant's entire argument rests upon the false basis of these incorrect statements. For this reason authorities under each of his points have no application to the facts of the case.

After stating appellants' contentions as to why respondent had no right to deduct the said sum of \$221,610.87 paid to the County Treasurer to meet such interest charges, the Tax Court in its opinion summarized appellant's fallacious reasoning and respondent's right to make such deduction in the following words:

*"The essential factual premises or inferences which respondent assumes for this argument are not adequately supported by the evidence. We can disregard as negligible the 240 district acres which petitioner did not own and against which an assessment for bond interest apparently was not made, but we can not lightly ignore a public district invested with taxing powers and other sovereign attributes and the substance attaching to the very large number of bonds which were held by parties who had no identity of interest with the Birches and whose right to bond interest was consistently observed, in one case, after threat of suit. The Hopkins sisters acquired 786 of the 2000 bonds in 1925; they owned 310 from 1931 to March 15, 1944, or during five and a half months of fiscal 1944. At an undisclosed date the Birches sold 86 bonds to the Great Republic Life Insurance Co., and its successor sold these bonds to petitioner in 1940; the Birches sold 10 bonds to Lula Minter who held them throughout fiscal 1944. Peti-*

tioner regularly paid to the Hopkins sisters and to Lula Minter the amount of accrued interest due them, receiving and turning over the interest coupons to the County Treasurer. By so doing it acquired a credit in the same amount on the district's assessment for interest. See section 11, article II, chapter 1, Title 8, Part 8, Political Code of California, and hence it is not technically correct to say that no assessment taxes were paid from 1937 to 1944. An amount of \$19,200 was paid each year, and by this Court's decision in Docket No. 109993 the amounts so paid were deductible." [R. 403.] (Emphasis added.)

**A. The \$221,610.87 Paid by Taxpayer Constituted Taxes Assessed Against Local Benefits.**

In his argument, appellant overlooks the fact that a Reclamation District is a separate legal entity and a *quasi* public corporation, separate and apart from the land owners, even if all of the land in the district were owned by a single owner, which at the time of the formation of the district and the construction of the improvements in the district was not the situation here. [R. 134-138.]

At the time of the formation of the district and the approval of the plans by the Reclamation Board of the State of California, there were eight other land owners in the district, and the improvements were made entirely separate and apart by Mr. and Mrs. Birch and Mr. and Mrs. Conaway, as contractors, entirely separate and apart from the district. [Stipulation of Facts, R. 134-138.]

In 1920 the Commissioners of Assessment, duly appointed, assessed the value of the benefit to the lands in the district from the improvements contemplated and ap-

portioned the cost of such improvements according to the benefits that would accrue to each of the nine tracts of land then comprising the district. [R. 137.] The issuance of the bonds did not occur until five years later. [R. 139.]

Certainly when this assessment was made, the assessment was a bona fide assessment duly made and the Reclamation District was a bona fide district duly organized. Also, the bonds thereafter issued were duly issued and constituted a valid lien against the lands of the district. Under the laws of the State of California for such cases specially provided the Superior Court of Yolo County so held. (Statement of the Case, *supra*, and Section 3478 of the California Political Code.)

There is no question here even of any intention of tax avoidance.

Mr. Birch testified as follows:

“Q. (By Mr. Acret): Mr. Birch, in participating as one of the landowners (170) in the formation of Reclamation District No. 2035, did you or your associates have any intention of tax avoidance?

A. No, it never occurred to us.

\* \* \* \* \*

Q. Did you in any way have any intention of tax avoidance in connection with that matter? A. None whatever. (171.)

Q. How long was it that you waited for your money for the work that you and Mr. Conaway did in improving the district from the time of the commencement of the work until the time that you got the money or the bonds in payment therefor? A. About six or seven years. [R. 297.]

\* \* \* \* \*

Q. Did you, yourself, receive any advice from any attorney or accountant with respect to the tax phrase of that matter, prior to the organization of any reclamation district? A. No, and, furthermore, we didn't have any thought in mind of ever getting out a bond issue.

Q. How did you learn of the tax exempt phase of that matter, if you can recall, back when it first came to your attention? That was a matter of State law, of course, but when did that first come to your attention? A. After we received the bonds in 1925.

Q. You did not know of it, then, before that time? A. No." [R. 337-338.]

Appellant overlooks the fact that in constructing and developing for the district 45 miles of roadways and 47 miles of irrigation canals and 55 miles of drainage canals and ditches, the landowners in the district constructed and developed rights of way and so forth which became a part of the Reclamation District and property rights entirely separate and apart from the lands owned by the various owners in the district, including the Conaway ranch.

In *Western Insurance Company v. Drainage District 72*, 72 Cal. App. 68, 72, it is held that though the administration of the affairs of reclamation districts is committed entirely to the owners of the lands embraced within the districts, that nevertheless such districts are "public mandatories and governmental agencies through which the state administers and executes one of its most important functions."

Appellant overlooks not only the record facts but also all the requirements and provisions of the Reclamation Act, to-wit, Section 3480 of the California Political Code, the applicable portions of which are set forth as Appendix B



to this brief. This Act provides for the manner of the formation of a reclamation district; the issuance of bonds; the validation of these bonds; the assessment of lands in the district to meet the expenses of the district, including payment of interest on these bonds; and for the payment of all moneys collected from such assessments *into the County Treasury*; for all unpaid installments of assessments to constitute a lien upon the lands in the district until paid, and permitting the land owners to pay the assessment installments, either in cash or with the interest coupons of the bonds.

The Reclamation District is a separate legal entity, and under the laws of the State of California, the County Treasurer in behalf of such separate entity was obliged to collect the principal and interest of the assessment against the taxpayer's lands and to maintain a lien against such lands until such principal and interest is paid and to foreclose such lien if and when the payment of such principal and interest is in default.

Regardless of all of the foregoing, as pointed out by the Tax Court's decision, the bona fide character of the bonds, the varied character of their ownership, and their having been extensively dealt in for value over a long period of years, is in itself alone a sufficient reason to remove all question of the payor and the payee on the bonds being economically identical, and to remove all question as to the right of the taxpayer to make the deduction involved herein.

Even if all of the lands in the district had been owned by the taxpayer, and the taxpayer had owned all, or most, of the bonds, nevertheless it would have been entitled to deduct the money it paid to the County Treasurer to meet

the interest accrued on the bonds. The provision for the issuance of bonds, the income from which was exempt from taxation, contemplated just such a situation and the possibility of the ownership of the bonds by the owner of the lands in the district. The purpose was to encourage, *and coerce*, reclamation of marginal and swamp lands in the state of California and to hold out the advantage of exempt bonds even if the taxpayer should own *all* of the lands in the district and *all* of the bonds, which however does not happen to be the situation of ownership in the instant case.

In the case of *Western Assur. Co. v. Drain Dist.*, 72 Cal. App. 68, 72, it is stated as follows:

“ . . . Some of the drainage and reclamation and irrigation districts considered by the cases just mentioned were formed and organized under special acts of the legislature and some under the general laws of the state, and, while the administration of the affairs of all of them is committed entirely to the owners of the lands embraced within the districts, still they are, nevertheless, public mandatories or governmental agencies through which the state administers and executes one of its most important functions. The reason that that is so as to reclamation districts is because the swamp and overflowed lands of California were granted by the general government to the state upon condition that the latter would see to the reclamation of the same so that they might become suitable for the purposes of cultivation, and, as an essential corollary of that proposition, those who purchase such lands from the state so take them subject to the right, and, indeed, the duty of the state, either by a scheme immediately directed and supervised by itself through officers or agents appointed for that purpose, or by committing that duty to the owners themselves of such

lands, to coerce such reclamation according to such rules, regulations, and plans as may be prescribed by the state through its legislature.” (Emphasis added.)

The provisions of the Reclamation Act itself disclose this intention. Section 3480 of the Political Code provides:

“Any landowner of the district *who shall desire at any time to lessen or remove the lien upon his land of any assessment on which bonds have been or hereafter may be issued may deliver to the County Treasurer for cancellation any bonds payable out of said assessment, and the Treasurer shall credit against the assessment on his land the principal and accrued interest of said bonds.*” (Emphasis added.)

Regardless of the ownership of the bonds, of the ownership of the lands, or the taxpayer's intentions, in order to avail itself of the express provisions of the laws of the State of California with respect to reclamation districts and reclamation bonds, it was entitled to deduct moneys paid to the County Treasurer to meet interest on the bonds and to treat as exempt such moneys when received back from the County Treasurer.

The foregoing constitutes obviously some of the reasons as to why from 1925 to 1934, while Mr. and Mrs. Birch owned all of the lands in the district except 240 acres, and while they owned a little more than half of the bonds, they were permitted by the Commissioner to deduct all of the money paid to the County Treasurer to enable the district to meet interest on all of the bonds, including the bonds owned by themselves, and at the same time they were not obliged to account to the government for this money as

income when it was paid back to them by the County Treasurer as interest from the bonds.

After the State of California holds out to its citizens the tax advantages resulting from the development of marginal and swamp lands and of the issuance of bonds to cover the cost of such development, in order to encourage such development, it would seem to be an act of bad faith for the government to attempt to deprive the taxpayer of such advantages.

From the foregoing it appears that respondents' reasons for the assessment not constituting an assessment for local benefits is fallacious, as well as being unsupported by the facts.

**B. The \$221,610.87 Is Deductible Because It Is Not "Interest Paid" but "Taxes Paid" to Meet Interest Charges With Respect to Assessments Against Local Benefits.**

The Tax Court in its opinion stated as follows:

"Principal and interest were payable out of moneys collected by the treasurer of Yolo County from assessments against the benefited lands, which assessments were to be deposited 'into the main county treasury,' but 'credited to the bond fund' of the District, as provided by Section 3480, Article II, c. 1, Title 8, Deering's Political Code of California. [R. 389-390.]"

From the said Section 3480 and from the argument under the preceding sub-heading, it would seem that the above-quoted statement is clearly correct. The Birches and the Conaways had a right to act, as contractors, in constructing the improvements upon the various rights of way of the District, the same as any other persons, and



they had a right to be paid for such work by the issuance of a warrant, and under the laws of the state to have bonds issued in payment of such warrant. After the bonds were issued, nearly half of them became owned by various third parties, and for over a period of more than twenty years such bonds as to their principal and interest, with one small exception, were dealt in upon the basis of their face or par value.

There is no similarity whatsoever in the facts in this case to the facts in any of the cases cited by petitioner.

As held in the case of Andrew Little, *supra*, the payment to the County to meet interest on such bonds constitutes a payment of taxes and not interest within the meaning of a similar section of the then existing Revenue Act.

During all of the period involved in this action, nearly half of the bonds were owned in arm's length transactions by third parties, and even if the bonds had all been owned by taxpayer, the payor and the payee were not economically identical. The intervening party was a bona fide reclamation district of the State of California, the financial agent of which was the County Treasurer of Yolo County, who was obliged to act under the provisions of said Section 3480 of the Political Code.

As argued under a previous point, the Reclamation Act itself contemplates that the landowner in the district may own the bonds. It provides that he *may* remove the lien of the bond upon his land if he "*shall desire*" by turning in the bonds *at any time* to the County Treasurer. There is no requirement in the Act that he shall turn in the bonds at any time.

As heretofore shown, the purpose of the provision that the income from reclamation district bonds shall be exempt from taxation was in order to encourage the development of marginal lands in California. It was in order to "coerce" the development of such lands. Also heretofore shown, the statute expressly provides that such bond issues may be refunded, and the refunding of such bond issues is a common practice in the State of California. As also heretofore shown, however, in the instant case the bond issue was refunded, and there was delay in providing the money to pay for some of the bond interest coupons, for the reason that the taxpayer had been connected with a bank which failed, and until 1944 it was without sufficient money.

**C. The Taxpayer's Deduction of the Payment of \$221,610.87 as Taxes Is Not in Conflict With the Purpose of Section 122(d)(2) for the Reason That Such Payment Was for Taxes Actually Due and Payable, and Which in Fact Did Constitute an Economic Loss.**

The argument under this point is covered not only by the facts of the case as heretofore stated, but by the statements contained under previous points.

If the taxpayer had not met the call of the County Treasurer to enable him to pay the matured interest coupons upon the bonds owned by the Hopkins, Miss Minter, and the Republic Life, which constituted close to one-half of the entire bond issue, such owners would have caused the entire bond issue to be foreclosed. As to the payment of the calls to meet the interest accruing on these bonds, and as to the taxpayer's purchase of matured in-

terest coupons of these bonds, it suffered an economic loss. As to the taxpayer's payment of that portion of the call which related to an amount of money sufficient to pay the interest coupons owned by the Birch Securities Company, the taxpayer in fact also suffered an actual economic loss in view of the intervention of the County Treasurer. Under the provisions of the statute all of the money so paid went into the general fund of the County Treasury and the County Treasurer was obliged to pay it out to any holder of interest coupons whomever he might be.

As stated by the Tax Court:

"The funds which the district collected by its assessment calls were for the payment of interest in general, and we are of opinion that petitioner's right to deduct its payments as a tax is not defeated by the fact that a part of such payments became available to pay interest on bonds held by it, by Securities, by Holding, or by the Birches. Andrew Little, 21 B. T. A. 911.

"Respondent argues further that the 'payments of interest on reclamation bonds' was the payment of interest on indebtedness incurred and continued to purchase and carry tax-exempt obligations, and hence such payments are not deductible under section 23(b), Internal Revenue Code. Recognizing the reclamation district as a legal entity, we view petitioner's payments as made in satisfaction of taxes, not of interest, and the argument thus lacks factual foundation. As taxes assessed for interest only, they are not of a kind tending to increase the value of the property assessed, and are hence properly deductible. Mary E. Evans, 42 B. T. A. 246; Missouri State Life Insurance Co., 29 B. T. A. 401; Andrew Little, *supra*."

## POINT TWO.

The Reclamation District Being Regularly Formed by a Group of Eight Property Owners in Addition to the Birches, and the Bonds Having Been Regularly Issued to Pay for Improvements of a Bona Fide Value in Excess of \$2,000,000, Such District and Such Bonds Did Not Lose Their Bona Fide Character by Reason of the Subsequent Acquisition by Respondent Corporation, as the Birches' Successor in Interest, of Practically All of the Land in the District and a Substantial Portion of the Bonds.

It would seem that the correctness of the above statement would be obvious.

To take a somewhat similar illustration, if the Birches had owned lots in two city blocks and had caused the city, in a street proceeding, to pave the street running between those two blocks and to assess the cost thereof against the lots in each of the blocks, and had caused ten-year bonds to be issued against the two blocks in the district, surely it would not be contended that the street improvement district and the bonds had become identical because of the Birches' subsequent acquisition of all but one of the lots and more than one-half of the bonds. Nor could it be so contended even if the Birches had acquired all of the lots and all of the bonds.



### POINT THREE.

Where Respondent's Predecessor in Interest, Mr. Birch, Was Nearly Seventy Years Old and During the Depression Could Not Get Bank Credit Sufficient to Enable Him to Operate the Ranch Unless He Placed the Title Thereof in a Corporation, and Where the Taxpayer Corporation Was Formed for the Purpose of Securing Such Bank Credit, There Is No Question of Alter Ego, and the Corporation Is an Entirely Separate Legal Entity With Respect to Taxation, as Well as in Every Other Respect.

It is immaterial as to whether the Birch Securities Company, which owned the bonds, was the *alter ego* of the Birches. It is sufficient that respondent, the Birch Ranch and Oil Company, is a separate legal entity.

As heretofore shown the parties stipulated as follows:

"17. On October 15, 1934, Birch and his wife organized Birch Ranch and Oil Company, the petitioner herein, and transferred to it the Conaway Ranch, their interest in the Birch Oil Company, the partnership which succeeded the Menges Oil Company in 1911, and all other property belonging to them, except the bonds of Reclamation District No. 2035, certain corporate stock and other properties having a value of about \$600,000. Birch had been having difficulties during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, and the petitioner was organized for the purpose of procuring needed bank credit."

It would seem that there could be no possibility of respondent being the mere business conduit and *alter ego* for the Birches. At the time they formed the company, they merely turned over to it the title to the lands comprising the Conaway ranch. They held out, and kept in their own names, the title to properties having a value of about \$600,000 [R. 143] and this property never did go into the corporation. "Birch had been having difficulty during the depression years in borrowing on his personal credit the moneys needed for the operation of the ranch, and (the taxpayer) was organized *for the purpose of procuring needed bank credit.*"

It would be difficult to conceive of a corporation being organized in a manner sufficient to constitute a separate legal entity under more compelling facts and circumstances.

The very purpose of a corporation is to enable it to enjoy credit separate and apart from the risk of the personal indebtedness of its shareholders, with respect to taxes, as well as in every other respect. Certainly, business houses and banks ought to be free to extend credit to such a corporation without the corporation becoming liable, or mixed up in any respect whatsoever, with the personal indebtedness of the Birches, or any of their other companies, with respect to taxes or any other indebtedness. If this were not so, corporate credit, and the backbone of free enterprise in America, could not exist.

This point, though quite unnecessary, would seem to be compelling.

**Conclusion.**

It would seem that the decision of the Tax Court ought to be upheld and the petition herein denied.

Respectfully submitted,

GEORGE ACRET,

*Attorney for Respondent.*







## APPENDIX A.

### BOND OF RECLAMATION DISTRICT 2035

United States of America

State of California

County of Yolo

Number

2000

Dollars

1000

Reclamation District

No. 2035

Reclamation District No. 2035 for value received hereby acknowledges itself indebted to and promises to pay to the holder hereof at the office of the treasurer of said County in State of California, on the first day of January, 1943 the sum of

One Thousand Dollars (\$1000.00)

in gold coin of the United States of America, with interest thereon in like gold coin from date hereof until paid, at the rate of six per cent. per annum, payable at the office of said treasurer semi-annually on the first day of January and the first day of July in each year on presentation and surrender of the interest coupons hereto attached. This bond is one of a series of 2265 bonds of like tenor and effect as to denomination and maturity, numbered from 1 to 2265, inclusive, amounting in the aggregate to Two million two hundred sixty-four thousand seven hundred forty Dollars (\$2,264,740) issued in accordance with section 3480 of the Political Code of the State of California pursuant to an [235] election held in said

Reclamation District on the 28th day of August, 1924, authorizing its issuance, and is based upon and secured by an assessment levied on the lands in said district, and filed in the office of the county treasurer of said County of Yolo on the 23rd day of July, 1924, and the said Reclamation District does hereby certify and declare that said election was duly called and held upon due notice, and the result thereof was duly canvassed and ascertained in pursuance of and in strict conformity with the laws of the State of California applicable thereto, and that all of the acts and conditions and things required by law to be done, precedent to and in the issue of said bonds have been done and have been performed in regular and in due form and in strict accordance with the provisions of the law authorizing the issuance of reclamation bonds.

In Testimony Whereof, the said District, by its board of trustees, has caused this bond to be signed by the president of said board and attested by the auditor of said County of Yolo, with his seal of office affixed this 1st day of January, 1925.

C. HAROLD HOPKINS  
President of said Board

Attest:  
[Seal]

P. D. WALLACE  
Auditor of the County of Yolo  
State of California [236]

## APPENDIX B.

EXCERPTS FROM SECTION 3480 OF THE CALIFORNIA  
POLITICAL CODE, WITH APPROPRIATE EMPHASIS  
ADDED:

*Action to test legality.* At any time within thirty days after said bonds shall have been delivered to the treasurer of the county, an action may be commenced in the superior court of said main county by the trustees of said reclamation district in its name against the lands in said district and all persons owning the same or interested therein, to have it determined that said bonds are a legal obligation of such reclamation district, and in the event no such action is brought then the same may be commenced by any land owner in the district within thirty days thereafter. It shall be sufficient to describe said lands as all lands in the district (naming it), without a more specific description. The summons shall be published once a week for two weeks in some newspaper of general circulation published in the county where the action is pending. Within thirty days after the first publication of summons any owners of land in such district, or any person interested, may appear and answer the complaint, which answer shall set forth the facts relied upon to show the invalidity of said bonds. The default of all defendants not so appearing may be entered. Such action shall be given precedence in hearing and trial over all other civil actions in such court, and judgment rendered declaring such matter so contested either valid or invalid. Any party not in default may have the right to appeal to the Supreme Court within thirty days after the entry of judgment. Judgment for the plaintiff in such proceedings shall be considered as a judgment *in rem* and shall be conclusive against said



district and against all lands therein and all owners thereof and other interested persons.

\*   \*   \*   \*   \*   \*   \*   \*   \*

*Bond fund.* All moneys collected by any county treasurer upon any assessment upon which bonds shall have been issued, including all moneys derived from sale of land for delinquent installments, or from redemption thereof, or from sale of lands bought by the treasurer at any such sale, *shall be by such treasurer forthwith paid into the main county treasury* and except as otherwise provided in section 3466a of this code, shall be credited to the bond fund of such reclamation district and used exclusively for the payment of principal and interest of said bonds issued on such assessment, and of the principal and interest of any refunding bonds issued thereon, and the expenses of the county treasurer as hereinafter provided.

\*   \*   \*   \*   \*   \*   \*   \*   \*

*Additional assessment.* The lien of any unpaid assessment upon which bonds shall have been issued shall continue until all said bonds, and any refunding bonds which may be issued, shall have been paid in full except as hereinafter provided in reference to the use of bonds as payment of assessments, and if for any reason any part of such principal or interest of said bonds, or of refunding bonds shall remain unpaid after enforcement of said assessment as in this article provided, the board of supervisors of the main county shall order an additional or supplemental assessment to be made as provided in section 3459, sufficient to pay such unpaid principal and interest; which additional or supplemental assessment shall be enforced and collected in the same manner as the original assessment.

*Interest on unpaid installments.* Where bonds of the district have been authorized to be issued on such assessments all unpaid assessments shall bear interest at the rate of seven per cent per annum from the date of the bonds originally issued thereon until such bonds and any refunding bonds issued thereon shall have been fully paid and discharged, and the interest due at any time on said unpaid assessments may be called without calling any installment of the said assessment. The word installment as used in this section shall be construed as applying to interest as well as the principal as the case may be.

*Estimate of assessment installment to pay interest and principal.* At least ninety days before any interest date of the bonds, including refunding bonds, *the county treasurer of the main county shall estimate the amount of money necessary to pay interest and principal maturing on such interest date after crediting thereon the funds in the treasury applicable to the payment thereof*, and the expenses of the county treasurer hereinafter provided and shall add thereto fifteen per cent of such aggregate sum to cover possible delinquencies, and said county treasurer shall thereupon cause to be published two times, to wit: once a week for two weeks in some newspaper of general circulation published in each county in which any of the district may be situate a notice substantially in the following form: (Name of reclamation district.)

*Form of notice.* Notice is hereby given that *an installment of assessment* (describing it) of \$....., being .....per cent is payable within thirty days from (date) *by all assessed landowners* of said district in the county of (name of county) to the treasurer of said county. *All or any part of said installment which shall remain unpaid*

*on the day (day fixed) will be delinquent, together with ten per cent of such installment added as penalty.*

Dated (date).

(Signed).....,  
Treasurer of.....County.

If no newspaper is published in said county, such publication shall be made in a newspaper published in an adjoining county.

*Payment of installments: Delinquencies. Said installment may be paid either in cash or in bonds of said district, or their interest coupons, issued upon said assessment, then matured or to mature within ninety days from the date of the calling of such installment, taken at their face value, or part in cash and part in such bonds and/or coupons. Any bond or coupon so received in payment shall be by the treasurer forthwith canceled and filed in his office. If any part of such installment or any interest thereon shall remain unpaid at the expiration of thirty days from the date of said notice, it shall become delinquent and ten per cent of the unpaid amount of said installment shall be added thereto and collected by said treasurer.*

\* \* \* \* \*

*Sale for delinquent installments.* At the time stated in said notice, or such other time to which said sale may have been postponed, the county treasurer shall sell each parcel of land described in said notice to the highest bidder, unless prior thereto he shall have received payment in full of said delinquent installment together with such penalty.

\* \* \* \* \*

*Bonds as payment on assessment.* Any landowner of the district who shall desire at any time to lessen or remove the lien upon his land of any assessment on which bonds have been or hereafter may be issued may deliver to the county treasurer for cancellation any bonds payable out of said assesment, and the treasurer shall credit against the assessment on his land the principal and accrued interest of said bonds.

















